# SBA

SOP 50 10 8.1

# Lender and Development Company Loan Programs with Technical Updates

Office of Financial Assistance
U.S. Small Business Administration

# U.S. Small Business Administration

## Standard Operating Procedure
## Summary

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**Purpose:** Update SOP 50 10, Lender and Development Company Loan Programs

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**Stakeholders Affected:** All SBA employees and SBA Lenders

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**USER TIPS: HOW TO USE THIS DOCUMENT**

**SOP 50 10** contains the SBA's policies and procedures governing the 7(a) and 504 loan programs.

**This SOP** is divided into three sections.

Section A: Core Requirements for all 7(a) and 504 loans
Section B: 7(a) Loan Program requirements
Section C: 504 Loan Program requirements

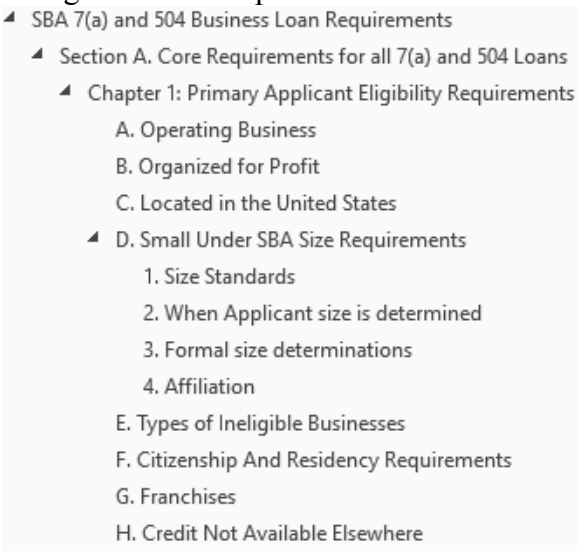
Navigating the SOP in Microsoft Word

The SOP contains bookmarks and built-in style headings to enable easy navigation using the Navigation Pane, which is a vertical panel on the left of the viewing screen. The Navigation Pane looks like a table of contents. Clicking on a line will jump you to the corresponding section in the SOP.

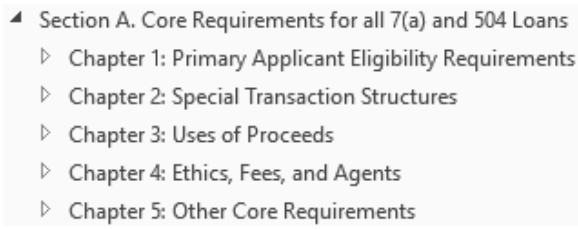
**Hint 1**: The sections expand and collapse by clicking on the arrows on the far left.

**Hint 2**: Clicking the "alt" and "left arrow" keys will return you to your original page when you click on a hyperlink that redirects you to a different place within the SOP. You may need to click your mouse once before you click the alt and left arrow keys.

Navigation Pane Expanded




Navigation Pane Collapsed




- Method 1: "CTRL+F" will launch a search screen. From here you can access the Navigation Pane by selecting Headings. You can also type in a keyword search here.
- Method 2: From the menu bar at the top of the screen, select "View," and then select the "Navigation Pane" box in the "Show" group.

**Want to see more tips?** Additional training is available on SBA's training on demand.

**SBA 7(A) AND 504 BUSINESS LOAN REQUIREMENTS**

Once an SBA Loan (defined as the full amount of the 7(a) loan or the Gross Debenture amount of the 504 loan) is disbursed, SBA Lenders must comply with the servicing and liquidation requirements in SOPs 50 57 (for 7(a) loans) and 50 55 (for 504 loans).

## Section A: Core requirements for all 7(a) and 504 loans: 7(a) Lenders and CDCs (SBA Lenders) must always start by reviewing the contents of this section. These core requirements apply to both 7(a) and 504 loan programs.

**Section B: 7(a) Loan Program Specific Requirements**: 7(a) Lenders must comply with the Core requirements in Section A and with the detailed guidance provided for each delivery method in the applicable chapter of Section B. Requirements for all 7(a) loans from the SBA Terms and Conditions through loan closing and disbursement are detailed in Chapter 6.

Chapter 1: Standard 7(a) Loans (Loans greater than $350,000)
Chapter 2: 7(a) Small & SBA Express
Chapter 3: 7(a) Manufacturers' Access to Revolving Capital (MARC)
Chapter 4: 7(a) CAPLines
Chapter 5: 7(a) Export Trade Finance
A. Export Express
B. Export Working Capital Program
C. International Trade
Chapter 6: SBA Terms and Conditions through Disbursement for all 7(a) Loans

**Section C: 504 Loan Program Specific Requirements**: CDCs must comply with the Core requirements in Section A and with the detailed guidance provided for the delivery of 504 Loan Program loans.

**Exceptions to Policy**: When the policy set forth does not adequately address the unique circumstances regarding a particular matter, the SBA Lender may submit a request for an exception to policy.

For the 7(a) Loan Program:

- Lenders that do **not** have delegated authority may submit requests for exceptions to 7aLoanProgram@sba.gov, and the loan will be processed under non-delegated procedures.
- Lenders that have delegated authority **must** make a request for an exception for **any** type of 7(a) loan to 7aDelegatedLoanApps@sba.gov, providing detailed information about the

application including the name of the Applicant, the names of the principals, address of the project, loan amount, delivery method, and a discussion of the policy for which the exception is being requested along with an explanation why the exception to policy should be granted. **Lender is to provide a summary of the facts - SBA will not be reviewing the entire case file or multiple attachments**.

- If SBA approves the exception, the Lender will receive an email confirming the approval, and the Lender must proceed to process the application under delegated authority. The Lender must retain the approval email in the loan file. Exceptions to policy will be considered on a case-by-case basis, and the decision will only apply to the specific request.

- The 7aDelegatedLoanApps@sba.gov email account is only for Lenders with delegated authority that have questions about a specific loan application and is not to be used for general policy questions, which should be sent to 7aQuestions@sba.gov. Lenders must indicate the loan amount and delivery method in their email.

For the 504 Loan Program, CDCs may request an exception to policy at the time of application in the credit memorandum. If the CDC requests an exception to policy after loan approval, or as a result of changes to an approved 504 project, a policy exception may be requested through the submission of a "327 action" for review.

The loan processing center or Headquarters team will analyze the request and make a recommendation to the D/FA or designee for 504 loans and for 7(a) loans, except Export Working Capital Program (EWCP), Export Express, and International Trade (IT) loans, or to the Director, International Trade Finance (D/ITF) for EWCP, Export Express, and IT loans. The D/FA or designee, or D/ITF, or an individual acting in that capacity, will make the final decision (with the concurrence of the D/OCRM for Export Express loans).

The D/FA or designee or D/ITF may not approve an exception to policy if such exception would be inconsistent with a statute or regulation. This procedure may only be used in situations where a minor deviation from standard policy is necessary for the specific situation. Exceptions to policy will be considered on a case-by-case basis, and the decision will only apply to the specific request. The decision must be documented in the appropriate Agency loan file.

**SECTION A. CORE REQUIREMENTS FOR ALL 7(A) AND 504 LOANS**

## Section A: Core requirements for all 7(a) and 504 loans:

7(a) Lenders and CDCs (SBA Lenders) must always start by reviewing the contents of this section. These core requirements apply to both 7(a) and 504 loan programs.

**NOTE:** "SBA Lender" is defined in 13 CFR § 120.10 as a 7(a) Lender or a CDC. This term includes SBA Supervised Lenders.

# CHAPTER 1: PRIMARY APPLICANT ELIGIBILITY REQUIREMENTS

Determination of Applicant eligibility is a required and critical step in the SBA loan process and should be completed and documented by the Lender as early as practicable.

This Chapter addresses the core program eligibility requirements that apply to all loans made under either the 7(a) or the 504 Programs. The Applicant must meet all core requirements at the time of application and throughout loan closing and disbursement. See Paragraph D of this Chapter for more information on size standards.

The SBA's lending programs qualify as "Special-Purpose Credit Programs" under the Equal Credit Opportunity Act (ECOA). This regulation stipulates that information pertaining to the Applicant's marital status, sources of personal income, alimony, child support, and spouse's financial resources can be obtained and considered in determining program eligibility. Therefore, the SBA Lender has the right to obtain the signature of an Applicant's spouse (whether an owner of the business or not) or other Person if it is required by Federal or State law or to obtain a valid lien on collateral or for other reasons to protect SBA and SBA Lender interests.

Eligibility requirements for all Applicants for SBA business loans are set forth in 13 CFR § 120.100 and are discussed below.

For all 7(a) and 504 loans, the Applicant and project must meet all Loan Program Requirements, defined in 13 CFR § 120.10 as requirements imposed upon Lenders or CDCs by statute; SBA and other applicable government-wide regulations; any agreement the Lender or CDC has executed with SBA or to which the Lender or CDC is subject; SBA Standard Operating Procedures (SOPs); Federal Register notices; official SBA notices and forms applicable to the 7(a) Loan Program, 504 Loan Program, the SBA Terms and Conditions issued and revised by SBA from time to time. For CDCs, this term also includes requirements imposed by Debentures, as that term is defined in 13 CFR § 120.802.

## A. OPERATING BUSINESS

13 CFR § 120.100(a) The Applicant must be an Operating Business (except for Eligible Passive Companies (EPCs)).

## B. ORGANIZED FOR PROFIT

13 CFR § 120.100(b) All Applicants must be organized for profit. Non-profit businesses are not eligible for SBA business loan assistance. For-profit subsidiaries of non-profits may be eligible.

1. To determine an Applicant's for-profit status, the SBA Lender may review the Applicant's organizational documents, for example:
    a. Articles of Incorporation/ Organization (filed with the Secretary of State or similar department in the state where the Applicant is organized);

b. Corporate bylaws and any amendments;

c. Partnership Agreements;

d. Association Bylaws; and

e. Tax Returns.

2. If all other eligibility requirements are met, 13 CFR § 120.110(a) permits for-profit subsidiaries of a non-profit to be eligible for SBA assistance.

   a. The SBA Lender must include the non-profit affiliate's receipts or employees, as applicable, when determining the for-profit entity's size, except the size of a business concern owned and controlled by a Native Hawaiian Organization (NHO) which is measured independent of its parent NHO, and of other concerns owned by the NHO based on common ownership, management, or the performance of common administrative services. 13 CFR § 121.103(b)(2).

   b. Loan proceeds must be used exclusively for the benefit of the for-profit business.

   c. If the non-profit affiliate owns 20% or more of the for-profit business but cannot or will not guarantee the loan, the for-profit business is not eligible.

## C. LOCATED IN THE UNITED STATES

13 CFR § 120.100(c) The Applicant must be located in the United States (including its territories and possessions).

1. The Applicant must be created, organized, or incorporated in the United States, its territories, or possessions, be located and primarily operate in the United States (including its territories and possessions), be authorized to conduct business in the state, territory, or possession where it seeks SBA financial assistance, pay taxes to the United States (unless exempt, as in certain businesses in Puerto Rico and elsewhere), and to the extent practicable, purchase only American-made equipment and products with the proceeds of the SBA loan.

2. If an Applicant operates internationally, the loan proceeds must be used exclusively for the benefit of the U.S.-based Borrower (as a result, the business and its employees are subject to U.S. and local taxes).

3. Businesses involved in international trade are subject to U.S. trade restrictions. A 7(a) or 504 loan may not be made to a business that directly or indirectly exports to a foreign country which is listed as a prohibited country (Note # 7 on the Country Limitation Schedule | EXIM.GOV), or if the transaction would be prohibited under any of the sanctions programs administered by OFAC.

## D. SMALL UNDER SBA SIZE REQUIREMENTS

The Applicant must qualify as small under 13 CFR § 120.100(d) and SBA Size Requirements (13 CFR Part 121) (including affiliates). The Applicant may qualify under either the Industry Size Standards or the Alternative Size Standard.

1. Size Standards

    a. "Industry Size Standard." The Applicant alone (without affiliates) must not exceed the small business size standard for the industry in which the Applicant is primarily engaged, and the Applicant, when combined with its affiliates, must not exceed the size standard designated for either the primary industry (defined in 13 CFR § 121.107) of the Applicant alone or the primary industry of the Applicant and its affiliates, whichever is higher. SBA calculates annual receipts for both the Applicant and its affiliates based on Federal tax returns (13 CFR § 121.104). The table of size standards is found at 13 CFR § 121.201.

    b. "Alternative Size Standard." The Applicant (including affiliates) must meet the following (13 CFR §121.301):

        i. The maximum tangible net worth may not exceed $20 million; and

        ii. The average net income after Federal income taxes (excluding carry-over losses) for the 2 full fiscal years prior to application may not exceed $6.5 million.

    c. The applicable size standards are increased by 25 percent when the Applicant agrees to use all of the financial assistance within a labor surplus area (labor surplus areas are designated by the Department of Labor). (13 CFR § 121.301(e))

2. When Applicant size is determined

    (13 CFR § 121.302)

    a. Applicant size is determined as of the date the application is accepted for SBA processing; subsequent increases in size will not affect eligibility.

    b. For 7(a) and 504 loans involving a business acquisition or change of ownership, the combined size of the Applicant and the acquired business must meet applicable size standards.

    c. For applications processed under an SBA Lender's delegated authority (PLP, SBA Express, Export Express, PLP-EWCP, and PCLP CDC), the size of the small business is determined as of the date of approval of the loan by the SBA Lender.

3. Formal size determinations

    a. By signing the application, an Applicant has certified that it is small under the applicable small business size standard. SBA or the SBA Lender may request additional information concerning the Applicant's size based on information

supplied in the application or any other source. SBA or an SBA Lender processing a loan under delegated authority may accept as true the size information provided by an Applicant, unless credible evidence to the contrary is apparent. (13 CFR § 121.303)

b. Prior to denial of eligibility based on size, a formal size determination may be requested by an Applicant or the SBA official with authority to take final action on the assistance requested. (13 CFR § 121.1001(b)(1))

c. The SBA official may also request a determination of whether affiliation exists between an Applicant for financial assistance and one or more other entities to determine whether the Applicant, together with any affiliates, would exceed the maximum loan amount and maximum guaranty amount set out in 13 CFR § 120.151.

d. The request for a size or affiliation determination must be made to the Government Contracting Area Director serving the area in which the headquarters of the Applicant is located, regardless of the location of the parent company or affiliates.

4. Affiliation

13 CFR § 121.301

The Small Business Act defines a small business concern as one which is independently owned and operated, and which is not dominant in its field of operation. SBA interprets this statutory definition to require, in certain circumstances, the inclusion of other entities ("Affiliates") owned by the applicant or an owner of the applicant in determining the size of the applicant.

On April 10, 2023, SBA published the Final Rule on Affiliation and Lending Criteria for the SBA Business Loan Programs (88 FR 21074, effective May 11, 2023). This rule removed the principle of control, both affirmative and negative control, as establishing affiliation between entities. However, except for management agreements that are part of the franchise disclosure documents for a brand listed on SBA's Franchise Directory, franchise, license, or similar agreements (e.g., management agreements) must be reviewed to determine whether they give someone other than the Applicant the sole discretion to manage the operations of the business, including decision-making over the employees, the finances and the bank accounts of the business, with no involvement by the owner(s) of the Applicant, because this would cause the Applicant to be an ineligible passive business.

The following principles apply for the Business Loan, Disaster Loan, and Surety Bond Guaranty Programs:

a. Affiliation Based on Ownership

NAICS codes can be found at 13 CFR § 121.201, and a searchable database of industries and NAICS codes is located at naics.com and North American Industry Classification System-U.S. Census.

i. When the Applicant owns more than 50 percent of another business, the Applicant and the other business are affiliated.

ii. When a business owns more than 50 percent of an Applicant, the business that owns the Applicant is affiliated with the Applicant. Additionally, if the business entity owner that owns more than 50 percent of the Applicant also owns more than 50 percent of another business that operates in the same 3-digit NAICS subsector as the Applicant, then the business entity owner, the other business and the Applicant are all affiliated.

iii. When an individual owns more than 50 percent of the Applicant and the individual also owns more than 50 percent of another business entity that operates in the same 3-digit NAICS subsector as the Applicant, the Applicant and the individual owner's other business entity are affiliated.

iv. When the Applicant does not have an owner that owns more than 50 percent of the Applicant, if an owner of 20 percent or more of the Applicant is a business that operates in the same 3-digit NAICS subsector as the Applicant, the Applicant and the owner are affiliated.

v. When the Applicant does not have an owner that owns more than 50 percent of the Applicant, if an owner of 20 percent or more of the Applicant also owns more than 50 percent of another business entity that operates in the same 3-digit NAICS subsector as the Applicant, the Applicant and the owner's other business entity are affiliated.

vi. Ownership interests of spouses and minor children must be combined when determining amount of ownership interest. Ownership interests are not combined when spouses and minor children have individual ownership interests in different businesses.

vii. When determining the percentage of ownership that an individual owns in a business, SBA considers the pro rata ownership of entities. For example, John Smith, Jane Doe, and Jane Doe, Inc., each own an interest in the Applicant. Jane Doe owns 15 percent of the Applicant, and she also owns 100 percent of Jane Doe, Inc. Jane Doe, Inc. owns 50 percent of the Applicant. SBA considers Jane Doe to own 65 percent of the Applicant.

b. Affiliation Based on Stock Options, Convertible Securities, and Agreements to Merge

i. For purposes of this subparagraph, SBA considers stock options, convertible securities, and agreements to merge (including agreements in principle) to

have a present effect on the ownership of the entity. SBA treats such options, convertible securities, and agreements as though the rights granted have been exercised.

ii. Agreements to open or continue negotiations towards the possibility of a merger or a sale of stock at some later date are **not** considered "agreements in principle" and are thus not given present effect.

iii. Options, convertible securities, and agreements that are subject to conditions precedent which are incapable of fulfillment, speculative, conjectural, or unenforceable under state or Federal law, or where the probability of the transaction (or exercise of the rights) occurring is shown to be extremely remote, are not given present effect.

iv. SBA will not give present effect to individuals', concerns', or other entities' ability to divest all or part of their ownership interest to avoid a finding of affiliation.

c. Determining the Concern's Size

i. In determining the concern's size, SBA counts the receipts, employees (see 13 CFR § 121.201), or the alternate size standard (if applicable) of the concern whose size is at issue and all of its domestic and foreign affiliates, regardless of whether the affiliates are organized for profit.

ii. Exceptions to Affiliation - For exceptions to affiliation, see 13 CFR § 121.103(b).

## E. TYPES OF INELIGIBLE BUSINESSES

The SBA Lender must determine whether the Applicant is one of the types of businesses listed as ineligible (13 CFR § 120.110). Certain business types appearing on this list may be eligible under limited circumstances, as discussed below.

1. Non-profit businesses are ineligible (for-profit subsidiaries may be eligible). 13 CFR § 120.110(a)
2. Businesses Engaged in Lending 13 CFR § 120.110 (b).
    a. SBA cannot guarantee a loan that provides funds to businesses primarily engaged in lending, investment, or to an otherwise eligible business engaged in financing, factoring, or investment not related or essential to the business. This prohibits SBA Loans to:
        i. Banks;
        ii. Life Insurance Companies (but not independent agents);

iii. Finance Companies;

iv. Factoring Companies;

v. Investment Companies;

vi. Bail Bond Companies; and

vii. Other businesses whose stock in trade is money.

b. Certain businesses engaged in lending may be eligible under limited circumstances:

i. A pawn shop is eligible if more than 50 percent of prior year revenue is from merchandise sales rather than interest on loans.

ii. A business that provides financing in the regular course of its business (such as a business that finances credit sales) is eligible, if less than 50 percent of its revenue is from financing its sales.

iii. A mortgage servicing company that disburses loans and sells them within 14 calendar days of loan closing is eligible. Mortgage companies primarily engaged in the business of servicing loans are eligible. Mortgage companies that make loans and hold them in their portfolio are not eligible.

iv. A check cashing business is eligible if it receives more than 50% of its revenue from the service of cashing checks.

v. A business engaged in providing the services of a financial advisor on a fee basis is eligible, provided they do not use loan proceeds to invest in their own portfolio of investments.

3. Passive Businesses 13 CFR § 120.110(c):

a. Businesses owned by developers and landlords that do not actively use or occupy the assets acquired or improved with the loan proceeds are not eligible, except Eligible Passive Companies under 13 CFR § 120.111.

b. Businesses primarily engaged in subdividing real property into lots and developing it for resale on its own account are not eligible.

c. Businesses that are primarily engaged in owning or purchasing real estate and leasing it for any purpose are not eligible.

i. Shopping centers, office suites (aka salon suites), ghost kitchens, and similar business models that generate income by renting space to accommodate independent businesses that provide services directly to the public are not eligible unless all of the following apply:

a) The revenue is earned through membership dues (not rent); and

b) The business's customers do not have an assigned space that they know

they can return to each time they visit (i.e., customers do not get an office with a lockable door or a particular kitchen setup and the space cannot be personalized); and

c) The business is responsible for upkeep and maintenance and is supplying the equipment necessary for a fully functioning office/kitchen where customers can drop in and begin working. It is acceptable for customers to bring their own tools with them (e.g., kitchen knives).

ii. A business is either fully eligible or fully ineligible. If a business has a combined model (part of the revenue is from rent and part from membership dues or they provide for options where there is an assigned space model), it is not eligible.

d. Businesses that lease land for the installation of a cell phone tower, solar panels, billboards, or wind turbine also are not eligible. However, the business operating the cell phone tower, solar panel, billboard, or wind turbine is eligible.

e. Businesses that purchase a stand-alone asset that is operated on a passive basis are not eligible. Examples of these assets include standalone charging stations where there is no on-site operator.

f. Businesses that have entered into a management agreement with a third party that gives the management company sole discretion over the business operations are ineligible passive businesses. However, if the management company does not have sole discretion to manage the operations of the business and the Applicant exercises meaningful oversight of the business, the Applicant is eligible. "Meaningful oversight" by the Applicant means involvement in the decisions made concerning the operation of the business, which include a management agreement that provides for the Applicant to do all of the following:

i. Approve the annual operating budget;

ii. Approve any capital expenditures or operating expenses over a significant dollar threshold;

iii. Have control over the bank accounts; and

iv. Have oversight over the employees operating the business (who must be employees of the Applicant).

Regardless of whether processing the loan under delegated or non-delegated procedures, unless the management agreement is part of the franchise disclosure documents (FDD) for a brand listed on the Franchise Directory, SBA Lenders must review these agreements to determine whether the agreement makes the Applicant an ineligible passive business.

Note: Businesses that have entered into an agreement for control (including a side agreement) that gives a non-guarantor owner/investor control of the business are ineligible.

g. Apartment buildings and mobile home parks are not eligible.

h. Residential facilities that are not licensed as nursing homes or assisted living facilities and do not provide healthcare and/or medical services are not eligible.

i. The limited circumstances under which certain businesses engaged in renting or leasing may be eligible are as follows:

   i. Hotels, motels, recreational vehicle parks, marinas, campgrounds, or similar types of businesses are eligible if more than 50% of the business's revenue for the prior year is derived from transients who stay for 30 days or less at a time and the business complies with all zoning and other legal requirements. If the Applicant is a Start-Up Business, the Applicant's projections must show that more than 50% of the business's revenue will be derived from transients who stay for 30 days or less at a time. Rentals of residential or commercial space, whether through an internet platform that connects travelers with hosts or whether reservations are made directly with the owner, must be in compliance with all local laws and regulations, including zoning codes, and homeowners or condominium associations rules.

   ii. Businesses that are licensed as nursing homes, assisted living facilities, or state-licensed equivalents, and provide healthcare and/or medical services are eligible. Healthcare and/or medical services include but are not limited to services such as wellness checks, monitoring and/or helping take medications, monitoring blood sugar levels, and having medical staff onsite (even on a part-time basis). The SBA Lender must consider the terms of the license under which the business operates or will operate when determining eligibility.

   iii. Businesses that offer services which require professional licenses to operate are eligible, provided that the ownership structure meets all applicable state requirements in which they are located. If the business is under a franchise agreement, the business must meet all applicable franchise requirements. The Lender must document the eligibility of the business and ownership structure, per state requirements, in the loan file (e.g., medspas).

   iv. Businesses that are engaged in leasing equipment, household goods or other items are eligible. (See Subparagraph E.2. above regarding the eligibility of businesses engaged in lending.)

   v. Businesses such as barber shops, hair salons, nail salons, and similar types of personal services businesses are eligible, regardless of whether they have employees or contract with individuals to provide the services that the

business is providing directly to the public. (See subparagraphs a) and c) above regarding ineligibility of developers and landlords.)

vi. Businesses that provide a leveled model where the small business owner relies on the services of a middle level operator (e.g. cleaning service models) and does not have ownership of the contracts that support the business operation.

j. An ineligible business cannot obtain an SBA Loan for any purpose, including the purchase or construction of a building for its own use.

4. Life insurance carriers are not eligible. 13 CFR § 120.110(d)

5. Businesses located in a foreign country are not eligible. (See Paragraph F below for additional restrictions on Borrower ownership). 13 CFR § 120.110 (e)

6. Businesses using pyramid or multilevel sales distribution plans are not eligible. 13 CFR § 120.110(f)

7. Businesses that obtain more than one-third of their annual gross revenue for the prior year, including rental income, from legal gambling activities are not eligible. 13 CFR § 120.110(g)

   a. If the purpose of the business is gambling, such as a pari-mutuel betting racetrack, a gambling casino, or skill games (e.g. video poker) the business is not eligible, regardless of the percentage of gross revenue derived from gambling.

   b. Circumstances exist in which businesses engaged in legal gambling activities may be eligible, including if the Applicant obtains one-third or less of their annual gross revenue, including rental income from:

      i. Commissions from official State lottery ticket sales under a State license; or

      ii. Gambling activities licensed and supervised by a state authority in those states where the activities are legal.

8. Businesses that are engaged in any activity that is illegal under federal, state, or local law are not eligible. 13 CFR § 120.110 (h)

   a. Applicants that are engaged in illegal activity under federal, state, or local law are not eligible. This includes Applicants who make, sell, service, distribute, or promote products or services used in connection with illegal activity, unless such use can be shown to be completely outside of the Applicant's intended market. If the business sells products made from hemp or CBD or devices associated with consuming marijuana, the SBA Lender is responsible for obtaining from the Applicant documentation sufficient to demonstrate that the products sold by the business are not illegal under federal, state, or local laws.

   b. Marijuana:

Because federal law prohibits the distribution and sale of marijuana, financial transactions involving a marijuana-related business would generally involve funds derived from illegal activity. Therefore, businesses that derive revenue from marijuana-related activities may be ineligible for SBA financial assistance. The nature of the business's specific operations determines whether a business is eligible. The following businesses are ineligible: a business that grows, produces, processes, distributes, or sells marijuana or marijuana products, edibles, or derivatives, regardless of the amount of such activity. This also includes businesses that sell smoking devices, pipes, bongs, inhalants, or other products if the products are primarily intended or designed for marijuana use or if the business markets the products for such use. This applies to recreational use and medical use even if the business is legal under local or state law where the Applicant is or will be located.

c. Hemp: Consistent with the Agriculture Improvement Act of 2018 (Public Law No. 115-334), a business that grows, produces, processes, distributes or sells products made from hemp is eligible only if the hemp meets the definition in section 297A of the Agricultural Marketing Act of 1946 and any applicable state definition of hemp. (It is important to note that some states define hemp as having a lower level of THC than the federal definition.) The SBA Lender is responsible for obtaining from the Applicant documentation sufficient to demonstrate that the hemp meets the applicable definitions. In addition, for Applicants who will be growing, producing, and/or processing hemp, the SBA Lender is responsible for obtaining from the Applicant documentation of the testing protocols the business will follow to ensure that the hemp and any product(s) they extract or produce from it continue to meet the applicable definitions.

d. Cannabidiol (CBD): The factors to be considered in determining the eligibility of CBD-related businesses include, but are not limited to, the following:

   i. Where the CBD is derived from (whether from hemp or marijuana);

   ii. What types of products are being produced and/or sold (e.g., topical products or products to be ingested). Based on FDA guidance, it is illegal under the Food, Drug, & Cosmetic Act to add CBD to any food (human or animal), any dietary supplements, and certain cosmetics because cannabidiol is the active ingredient of an FDA-approved drug and has not been approved for other use. Please refer to FDA Regulation of Cannabis and Cannabis-Derived Products, Including Cannabidiol (CBD);

   iii. What health claims, if any, are being made about the product(s); and

   iv. Whether all products being produced and/or sold comply with all applicable federal, state, and local laws and regulations, including those issued by the FDA.

v. The SBA Lender is responsible for obtaining from the Applicant documentation sufficient to demonstrate that the products containing CBD being sold by the Applicant comply with all applicable federal, state, and local laws and regulations, including necessary certificates of lab analysis.

9. Businesses that restrict patronage for any reason other than capacity or that have discriminatory hiring practices are not eligible. 13 CFR §§ 120.110(i) and 113.3(a)

   a. Businesses that restrict patronage for any reason other than capacity are not eligible. For example, a men's or women's only health club is not eligible.

   b. Circumstances exist in which certain businesses, like fitness centers that market to one gender, may be eligible if they permit both men and women to join and/or use the facility. SBA Lenders must document the file with the following:

      i. Affidavit signed by the Applicant that the business is open to both men and women; and

      ii. Evidence that the facility is open to both men and women, such as appropriate bath/locker rooms, or documented membership demographics.

   c. Except as permitted under §702(a) of the Civil Rights Act of 1964 (42 U.S.C. § 2000e-1), businesses that have discriminatory hiring practices are not eligible. For example, a restaurant that employs only servers of one gender is not eligible.

10. Government-Owned Entities, except for businesses owned or controlled by a Native American tribe are not eligible. 13 CFR § 120.110(j)

    a. Businesses owned by municipalities and other political subdivisions are not eligible.

    b. Special Requirements Applicable to Native American Businesses:

       i. A Native American tribe is a Governmental entity and is not eligible.

       ii. A small business that is owned in whole or in part by a state or federally-recognized Native American Tribe may be eligible, provided the small business meets all other criteria set forth in SBA Loan Program Requirements and:

          a) Establishes that it is a separate legal entity from the tribe and submits the documents authorizing its existence; and

          b) For federally-recognized tribes, the tribe waives sovereign immunity with respect to the collateral pledged for the loan, and collection of the loan from the Applicant, AND agrees to a "sue and be sued" clause specifically naming U.S. Federal courts as "courts of competent jurisdiction." (Note: Tribes that are recognized only by a state do not have sovereign immunity. Therefore, this requirement is not necessary if the tribe is only recognized by a state.)

c. SBA Lenders may seek the advice and assistance of the Bureau of Indian Affairs (BIA) personnel when dealing with loans collateralized by Indian lands held in trust.

11. Loan Packagers, including Lender Service Providers, and other businesses earning more than one third of their gross annual revenue from packaging SBA loans are not eligible. 13 CFR § 120.110(m)

12. Businesses with an Associate who is currently incarcerated, serving a sentence of imprisonment imposed upon adjudication of guilty, or is under indictment for a felony or any crime involving or relating to financial misconduct or a false statement are ineligible. A business that is owned by an individual(s) who is currently on parole or probation may be eligible, but if the success of the business operations is primarily dependent on such individual, the Applicant must provide to the SBA Lender a plan for the continued operations of the business in the event of reincarceration, and the SBA Lender should consider whether it would be prudent, in order to protect SBA's and the SBA Lender's interests, to require an additional individual to provide a full or limited loan guaranty. 13 CFR § 120.110(n)

13. Businesses in which an SBA Lender or any of its Associates owns an equity interest, directly or indirectly, are not eligible. The only exception is when the Associate of the Applicant is a Small Business Investment Company (SBIC), in which case the requirements of 13 CFR § 120.104 apply.

14. Businesses that present live performances of a prurient sexual nature or that derive more than de minimis gross revenue, directly or indirectly, through the sale of products, services or the presentation of any depictions or displays of a prurient sexual nature. 13 CFR § 120.110 (p)

    a. SBA has determined that financing lawful activities of a prurient sexual nature is not in the public interest. The SBA Lender must consider whether the nature and extent of the sexual component causes the business activity to be prurient.

    b. A business is not eligible for SBA assistance if:

        i. It presents live or recorded performances of a prurient sexual nature; or

        ii. It derives more than 5% of its gross revenue, directly or indirectly, through the sale of products, services or the presentation of any depictions or displays of a prurient sexual nature. For this purpose, the 5% threshold is interpreted as the de minimis threshold for gross revenue.

15. Prior Loss to the Government 13 CFR § 120.110 (q)

    a. An Applicant is not eligible for a 7(a) or 504 loan if there is a prior loss to the Federal government. A "Prior Loss" has occurred when:

i. The Applicant has previously defaulted on a Federal loan or federally assisted financing, resulting in a loss to the Federal government or any of its agencies or departments; or

ii. Any other business owned, operated, or controlled by the Applicant or an Associate of the Applicant, previously defaulted on a Federal loan or federally assisted financing (or guaranteed a loan which was defaulted), resulting in a loss to the Federal government or any of its agencies or departments.

b. For purposes of this paragraph, "loss" means any deficiency on a Federal loan or federally assisted financing that has been incurred and recognized by a Federal agency after it has concluded its write-off and/or close-out procedures for the particular account and includes any amount compromised for less than the full amount, discharged through bankruptcy, and any unreimbursed advance payment under 8(a) or a similar program operated by a Federal agency.

NOTE: "Loss" does not include unpaid/delinquent taxes or any loss incurred by the Federal Deposit Insurance Corporation (FDIC) when it sells a loan at a discount.

c. "Federal loan or federally assisted financing" includes:

i. Any loan that is made for business purposes (including Federal disaster loans) by any Federal agency or department either directly or on a guaranteed basis; and

ii. Any advance payments under 8(a) or similar programs operated by any Federal agency.

NOTE: "Federal loan or federally assisted financing" does not include any loan purchased, held, or securitized by Fannie Mae or Freddie Mac or any Federal loan or federally assisted financing issued to an individual (e.g. student loan).

d. All SBA Lenders **must** check the Credit Alert Verification Reporting System (CAIVRS), to determine if the Applicant is ineligible for a 7(a) or 504 loan because the Applicant or a business owned, operated, or controlled by the Applicant or any of its Associates has a Prior Loss. SBA Lenders must retain documentation of the CAIVRS check in the loan file.

i. CAIVRS allows the SBA Lender to enter multiple tax identification numbers (either SSN or EIN) to conduct a search in connection with a loan application.

ii. SBA Lenders may access CAIVRS at https://entp.hud.gov/caivrs/public/home.html.

e. If a Prior Loss to the Government is fully satisfied, the application can be processed, including under an SBA Lender's delegated authority. The SBA Lender must document its file as to how the loss has been fully satisfied.

f. All SBA Lenders must inform the Applicant that if the small business defaults on the SBA-guaranteed loan and SBA suffers a loss, the names of the small business, the guarantors of the SBA-guaranteed loan, and any Associate(s) that control the Applicant, will be referred for listing in the CAIVRS database, which may affect the eligibility of a business owned or controlled by any such individual(s) or entity(ies) for future financial assistance from SBA or other Federal agencies or departments.

g. Exceptions to the Prior Loss rule: Non-controlling Minority Equity Investor: Under SBA's waiver authority at 13 CFR § 120.110 (q), a waiver may be granted for an Applicant whose owner was a Non-controlling Minority Equity Investor in a business that incurred a prior loss on an SBA 7(a) or 504 loan. To be eligible for this waiver, the aforementioned owner of the current Applicant must have:

   i. Held less than 20 percent of the equity of the business with the prior loss;

   ii. Was not a guarantor or co-borrower on the defaulted SBA 7(a) or 504 loan to that business; and

   iii. Did not have any control over the business with the prior loss

   For purposes of this paragraph, "Non-controlling Minority Equity Investor" means an owner of the current Applicant who satisfies paragraphs i. through iii. above with respect to the business that incurred the prior loss. Once these threshold criteria are met, SBA will evaluate the full circumstances surrounding the prior loss on a case-by-case basis, at the time of Application, through the Risk Mitigation Framework, using its discretion to determine whether granting a waiver is consistent with the purposes of the 7(a) and 504 programs. SBA will consider, among other factors: (i) the prior 7(a) or 504 loan(s) involving the Non-controlling Minority Equity Investor; (ii) the number and percentage of defaulted SBA loans involving the Non-controlling Minority Equity Investor; (iii) the timing of defaults (including whether a loan would have been considered an early default); and (iv) the Non-controlling Minority Equity Investor capital investment relative to the total SBA loan amounts. This waiver applies only to prior losses incurred under SBA Agency loan programs and does not apply to prior losses involving non-SBA Federal loans, other federally assisted financing, PPP loans, or SBA COVID-19 EIDL program loans.

16. Delinquent Federal Debt

31 CFR § 285.13

a. An Applicant is not eligible for a 7(a) or 504 loan if the Applicant or any

guarantor (except a Supplemental Guarantor) owes an outstanding nontax debt to the Federal Government, or any agency thereof, that is in delinquent status (hereafter referred to as "Delinquent Federal Debt").

b. A nontax debt owed to the Federal Government includes any amount of money, funds, or property that has been determined by an appropriate official of the Federal Government to be owed to the United States, or an agency thereof, by a person (including an individual, corporation, partnership or other type of entity), including debt administered by a third party as an Agent for the Federal Government.

c. A debt is in "delinquent status" when the debt has not been paid within 90 days of the payment due date. The payment due date is specified in the creditor agency's initial written demand for payment or other applicable agreement. A debt is considered "delinquent" even if the creditor agency has suspended or terminated collection activity with respect to such debt.

d. A debt is not considered "delinquent" if:

   i. The creditor agency has released the obligor from paying the debt or has agreed to accept a compromise amount in lieu of payment in full, or the obligor has cured the delinquency under terms acceptable to the creditor agency;

   ii. The obligor is subject to, or has been discharged from, the debt in a bankruptcy proceeding and, if applicable, the obligor is current on any court authorized repayment plan;

   iii. The obligor has entered into a satisfactory written repayment agreement with the creditor agency to pay the debt, in whole or in part, under terms and conditions acceptable to the creditor agency, and the obligor is paying as agreed; or

   iv. The debt is in an administrative or judicial appeal process.

   NOTE: If there was a Loss (as defined in Paragraph 15.b. above) associated with any of these debts, the Applicant remains subject to the Prior Loss rule.

e. SBA Lenders **must** check the Credit Alert Verification Reporting System (CAIVRS), to determine if the Applicant is ineligible for a 7(a) or 504 Loan because the Applicant, or any guarantor or Associate of the Applicant, has any Delinquent Federal Debt. CAIVRS allows the SBA Lender to enter multiple tax identification numbers (either SSN or EIN) to conduct a search in connection with a loan application. SBA Lenders may access CAIVRS at https://entp.hud.gov/caivrs/public/home.html. SBA Lenders must retain documentation of the CAIVRS check in the loan file.

f. If a Delinquent Federal Debt is fully satisfied, the application can be processed, including under an SBA Lender's delegated authority. The SBA Lender must document its file as to how the debt has been fully satisfied.

g. SBA does not routinely grant waivers under 31 CFR § 285.13. However, in the rare circumstance in which it is warranted, SBA may exercise its waiver authority as stated in 31 CFR § 285.13, Paragraph (g) Waivers by the agency. The regulation permits the authorized agency official to waive the eligibility requirement. The "authorized agency official" for purposes of the regulation is the head of the agency who may delegate this authority to the Chief Financial Officer, or Deputy Chief Financial Officer.

h. All SBA Lenders must inform the Applicant small business that if the small business defaults on the SBA-guaranteed loan and the Applicant is deemed to have a Delinquent Federal Debt, the names of the small business, the guarantors of the SBA-guaranteed loan, and the Associates of the small business, will be referred for listing in the CAIVRS database, which may affect their eligibility for further financial assistance from SBA or other Federal agencies or departments.

17. Businesses primarily engaged in political or lobbying activities are not eligible. 13 CFR § 120.110 (r) An Applicant that derives over 50% of its gross annual revenue from political or lobbying activities is not eligible.

18. Speculation 13 CFR § 120.110 (s)

    a. Speculative businesses are not eligible. This prohibits loans to an Applicant for:

        i. The sole purpose of purchasing and holding an item until the market price increases; or

        ii. Engaging in a risky business for the chance of an unusually large profit.

    b. Speculative businesses include:

        i. Wildcatting in oil;

        ii. Dealing in stocks, bonds, commodity futures, and other financial instruments;

        iii. Mining gold or silver in other than established fields;

        iv. Research and Development; and

        v. Building homes for future sale (except under the 7(a) Builders CAPLines program). Note: Construction of homes for future sale with no sales contract in place (spec homes) is eligible under the 7(a) Builders CAPLines program. 13 CFR § 120.391

    c. Non-speculative businesses that may be eligible include:

        i. A business, such as a grain elevator, that uses a commodity contract to lock in a price;

ii. A farmer who uses a commodity contract to lock in the sale price of his or her harvest;

iii. A business engaged in drilling for oil in established fields; and

iv. A business engaged in building a home under contract with an identified purchaser.

19. A Small Business Lending Company (SBLC) may not make a loan to an Applicant that has received financing (or a commitment for financing) from a Small Business Investment Company (SBIC) that is an Associate of the SBLC. 13 CFR § 120.476

20. Businesses located within the Coastal Barrier Resource System. 13 CFR § 120.175

21. The business is ineligible if the Applicant business has an existing 7(a) or 504 loan that is not current at the time of issuance of the new 7(a) or 504 SBA loan number. "Current" means that a required payment has not remained unpaid for more than 29 days. A loan that has matured and not been paid within 29 days of the maturity date is not current and is not eligible for refinancing. Note: The SBA Lender will see a "caution" pop-up when entering the application in the SBA Loan System if the business is delinquent on a 7(a) or 504 loan.

## F. CITIZENSHIP AND RESIDENCY REQUIREMENTS

SBA financing is limited to business Applicants with 100% direct and/or indirect owners and SBA-required guarantors, all of whom must be U.S. Citizens or U.S. Nationals who have their Principal Residence in the United States, its territories, or possessions. All entity owners (whether direct or indirect) must be created, organized, or incorporated in the United States, its territories, or possessions.

For any loan, SBA Lenders must certify in the SBA Loan System that, to the best of their knowledge, no direct or indirect owner or SBA-required guarantor is an "Ineligible Person" as defined in Appendix 3 of this SOP. No loan may be made if any direct or indirect owner or SBA-required guarantor is an Ineligible Person.

Direct/Indirect Owners: If a direct or indirect owner is an Ineligible Person, the business is ineligible unless the Ineligible Person completely divests their ownership prior to the date of issuance of the SBA loan number. Undocumented aliens who are in the U.S. illegally may not be an officer, director, or employee of the Applicant business.

Six-month lookback: The Applicant business is ineligible if any direct or indirect owner of the business commencing 6 months prior to the date of issuance of the SBA loan number is an Ineligible Person, unless the Ineligible Person completely divests their ownership interest prior to the date of issuance of the SBA loan number.

Guarantors (including Supplemental and Limited Guarantors): If any SBA-required guarantor (including an OC for a project structured as an EPC/OC), including direct and indirect owners, are Ineligible Persons, the Applicant is ineligible, with the following

exception for limited or supplemental guaranties. When a limited or supplemental guaranty is required by the Lender for their approval, or by SBA to support the pledge of jointly held required collateral, an Ineligible Person (except for undocumented aliens who are in the U.S. illegally) may provide a limited guaranty.

When the applicant business has other businesses that report their taxes on the Applicant business's tax returns, all the businesses on the tax return are subject to these requirements. However, affiliate businesses and partially owned subsidiaries that do not report their taxes on the Applicant business's tax returns are not subject to these requirements.

For servicing requests (e.g., substitution of an owner or SBA-required guarantor), the new individual may not be an Ineligible Person.

Eligible Persons: The following categories of individuals are eligible for SBA financing:

1. U.S. Citizens - Citizens born in an American territory: Generally, those born in an American territory are U.S. citizens. This includes but is not limited to the fifty U.S. states, the District of Columbia, Guam, Puerto Rico, the Commonwealth of the Northern Mariana Islands, and the U.S. Virgin Islands, but does not include outlying possessions of the United States (i.e., American Samoa and Swains Island).
2. U.S. Nationals - People born in American Samoa and Swains Island are considered U.S. Nationals at birth but are not automatically U.S. citizens. 8 U.S.C. § 1408 and 8 U.S.C. § 1101(a)(29). When making a loan to a business owned by a non-citizen U.S. National, the SBA Lender must document in the loan file that the SBA Lender has reviewed evidence of the person's status as a U.S. National (e.g., birth certificate or passport) and must enter the U.S. National's Social Security Number on the application and into the SBA Loan System.
3. Naturalized Citizens - Businesses owned by Naturalized Citizens are eligible, and the naturalized citizens are not subject to any special restrictions or requirements. No further verification of status is required if an individual is reflected as a U.S. Citizen on the SBA application.

Documenting Applicants' Eligibility: The SBA Lender must enter into the SBA Loan System 100% of the Applicant's direct and indirect owners, which includes entity and individual owners with direct or indirect ownership. SBA Lenders must also follow this process for guarantors and for servicing actions (e.g., for requests to substitute an owner or SBA-required guarantor). The ownership percentage of married spouses and minor children must be combined. SBA prohibits businesses where a minor child owns 20% or more of the business because minors are legally prohibited from providing a guaranty.

## G. FRANCHISES

1. The procedures described below apply to all agreements or relationships that SBA determines meet the Federal Trade Commission (FTC) definition of "franchise" in 16 CFR § 436. While a relationship established under a license, jobber, dealer or similar

agreement is not generally described as a "franchise" relationship, if SBA determines that the relationship meets the FTC's definition of a franchise, SBA will treat the relationship as a franchise. All such relationships are referred to in this paragraph as "franchises," the agreements are referred to as "franchise agreements," and the parties to such agreements are referred to as "franchisor" and "franchisee."

2. For purposes of determining whether an Applicant is operating under an eligible franchise, license, or similar agreement, SBA will only consider franchise, license, or similar agreements of the Applicant and not the agreements of any other franchisee or licensee owned or controlled by the Applicant.
3. Although exempt from FTC disclosure requirements, all agreements and relationships that are covered by the Petroleum Marketing Practices Act (PMPA), 15 U.S.C. 2801 *et al.* (e.g., gas stations with distributor, fuel supply, dealer and/or jobber agreements), are included within the FTC definition of "franchise" and are, therefore, subject to the procedures described below.
4. Applicants that are or will be operating under a dealer agreement with a new car manufacturer that meets the FTC definition of a franchise are subject to the procedures described below.
5. The SBA Franchise Directory:

   SBA has created the SBA Franchise Directory (the "Directory") of all franchise and other brands reviewed by SBA that are eligible for SBA financial assistance. The Directory will only include business models that SBA determines are eligible under SBA's eligibility criteria. Placement of a brand on the Directory is not an endorsement or a guaranty of the success of the brand.

   If the Applicant's brand meets the FTC definition of a franchise, it must be on the Directory in order to obtain SBA financing.

   To help minimize confusion over brands that may appear to be franchises but that do not meet the FTC definition, SBA will include such brands on the Directory at their request if they are eligible in all other respects. SBA Lenders will be able to rely on the Directory and will no longer need to review franchise or other brand documentation (except for management agreements that are not part of the franchise disclosure documents (FDD)) for eligibility.

   The Directory will be maintained on SBA's website and will contain the following information:

   a. Whether SBA determined that the brand meets the FTC definition of a franchise;
   b. The SBA Franchise Identifier Code, if applicable (a code will only be issued if the agreement meets the FTC definition of a franchise); and
   c. Whether there are additional issues the SBA Lender must consider with respect to

the brand (e.g., documentation that the business will be open to all, and review of any third party management agreement to ensure Applicant is not a passive business.

d. Use of the Directory by SBA Lenders:

i. For applications involving a franchise or similar relationship that meets the FTC definition of a franchise, SBA Lenders must check the Directory to determine if it includes the Applicant's brand before:

a) Submitting the application to SBA for non-delegated processing; or

b) Approving the loan under the SBA Lender's delegated authority.

ii. If the Applicant's brand is on the Directory:

SBA Lenders may proceed with submitting the application to SBA or approving the loan under delegated authority.

**iii. If the Applicant's brand is not on the Directory:**

a) For non-delegated loans, SBA Lenders cannot submit the application to SBA, and for delegated loans, SBA Lenders cannot approve the loan under delegated authority.

b) The SBA Lender should advise the Applicant and/or the franchisor of how the brand can be added to the Directory as detailed in paragraph e., Procedure to add brands to the Directory, below.

iv. Exception for Applicants Operating under Multiple Agreements:

a) When an Applicant operates under multiple agreements (i.e., multiple product lines), SBA Lenders first must check the Directory to ensure all of Applicant's agreements that meet the FTC definition of a franchise are on the Directory. **If any of the Applicant's agreements that meet the FTC definition of a franchise are not on the Directory, the application cannot proceed.**

b) If one of the Applicant's brands or agreements has been determined by SBA to be ineligible for SBA financial assistance, the loan cannot be processed, regardless of whether the brand or agreement meets the FTC definition of a franchise.

v. Exception for Applicants Operating under a Single, Non-critical Agreement: If the Applicant is operating under a single agreement that is not considered critical to the Applicant's business operation (i.e., it represents 50% or less of the Applicant's revenues), then the SBA Lender first must check the Directory to ensure that, if the Applicant's agreement meets the FTC definition of a franchise, it is on the Directory before processing the application. If the agreement meets the FTC definition of a franchise, but is

not on the Directory, the application cannot proceed. For example, the Applicant is an auto body shop that also rents trucks and trailers under an agreement. The rental of the trucks and trailers only represents 10% of the Applicant's revenues. The SBA Lender must check the Directory to ensure that, if the agreement meets the FTC definition of a franchise, the agreement is on the Directory. If the agreement is not listed on the Directory and the SBA Lender determines that the agreement does not meet the FTC definition of a franchise, the SBA Lender must determine the brand is eligible (e.g., does not have discriminatory hiring practices and is not an ineligible passive business) before proceeding with the application. SBA will make the final determination for non-delegated applications. For delegated applications, SBA will review the SBA Lender's determination at time of purchase or when conducting lender oversight activities for 7(a) loans and prior to closing for 504 loans. The delegated SBA Lender bears the risk of an incorrect determination on a delegated application.

e. Procedure to add brands to the SBA Franchise Directory:

   i. To add its brand to the Directory, a franchisor must submit the agreement, Franchise Disclosure Document (FDD) if applicable, and all other documents the franchisor requires the franchisee to sign to franchise@sba.gov for an eligibility determination. If the documents are submitted to SBA by someone other than the franchisor, contact information for the Franchisor (name and email address only) must be included in the email. The new brands are reviewed in the order in which they are received. Under certain circumstances, SBA as part of its review may request the franchise operations manual and other documentation explaining business operations.

   ii. The SBA Franchise Team will review the FDD and all other documents the franchisor requires that the franchisee to sign to determine if the business model is eligible under SBA's criteria. The Team will also assess whether the Franchisor has engaged in any illegal, fraudulent or other activity that SBA reasonably determines could be detrimental to SBA borrowers, or if the Franchisor is under any prohibited order from a State where they are not able to operate. The SBA Franchise Team will refer agreements involving brands that may be engaged in promoting religion, have activities of a prurient nature, that appear to cater to one gender, that were a party to litigation involving the federal government, or that present such other issues as the SBA Franchise Team may, in its discretion, deem appropriate, to the Associate General Counsel for Litigation for a final Agency decision on inclusion on the SBA Franchise Directory.

   iii. Upon completion of SBA's review and a determination by SBA that the brand is eligible, SBA will send the Franchisor Certification or the Distributor

Certification to the franchisor or distributor for review and an authorized representative's signature. Once a properly executed Franchisor or Distributor Certification is returned to SBA at franchise@sba.gov, SBA will list the brand on the Directory and will assign an SBA Franchise Identifier Code. If SBA determines that the brand does not meet the FTC definition of a franchise, SBA will list the brand on the Directory but will indicate that it does not meet the FTC definition of a franchise and SBA will not assign an SBA Franchise Identifier Code.

iv. If SBA determines that Franchisor/Distributor has not complied with the terms of the Franchisor/Distributor Certification or has engaged in any illegal activity, has submitted false information to SBA or the SBA Lender, or has withheld material information to SBA or the SBA Lender, or if a State has issued an order prohibiting the Franchisor or Distributor from operating within that State, SBA may remove the brand subject to a 30-day notice and opportunity for Franchisor/Distributor to respond. If SBA determines that Franchisor has not complied with the terms of the Certification, the brand is no longer eligible under SBA Loan Program Requirements, or for any other cause that warrants removal of the brand from the Directory, as determined by SBA in its discretion, SBA will provide the Franchisor with notice and 30 days to respond before removing the brand from the Directory.

f. Procedure to Submit Franchise Loan Applications:

i. For non-delegated loans, if the Lender does not have PLP authority:

a) If the Applicant's brand meets the FTC definition of a franchise, the SBA Lender must identify the name of the franchise and the SBA Franchise Identifier Code when entering the application into the SBA Loan System. The SBA Lender must ensure that the brand name (and where applicable, the type of agreement) the Applicant will be operating under matches the brand name (and where applicable, the type of agreement) listed on the Directory.

b) No other franchise documentation must be submitted to the SBA loan processing center with the application.

c) SBA will confirm that the brand is listed on the Directory.

d) If the SBA Lender determines that the Applicant's brand does not meet the FTC definition of a franchise, and it is not on the Directory, then the SBA Lender needs to explain its determination in its credit memorandum when submitting the application to the SBA loan processing center and provide the agreement and any additional documentation required by the brand. SBA Lender also must provide contact information for the franchisor/licensor (name and email address

only). The SBA loan processing center will forward the documentation and contact information to the SBA Franchise Team for review and final determination.

ii. For delegated loans:

a) If the Applicant's brand meets the FTC definition of a franchise, the SBA Lender must document in its file that the Applicant's brand is on the Directory and identify the name of the franchise and SBA Franchise Identifier Code when entering the application or request for loan number into the SBA Loan System. The SBA Lender must ensure that the brand name (and where applicable, the type of agreement) the Applicant will be operating under matches the brand name (and where applicable, the type of agreement) listed on the Directory.

b) The SBA Lender will need to submit the documentation showing that the Applicant's brand is on the Directory:

i) For 7(a) loans: With any guaranty purchase request;

ii) For 504 loans: To CDC closing counsel for Certification in the opinion of Counsel Letter prior to closing.

*c)* If the Applicant's brand is not on the Directory and the delegated SBA Lender determines the brand *does not meet the FTC definition:*

i) For 7(a) loans: If the SBA Lender proceeds with approving the loan under its delegated authority, SBA will review this decision at time of purchase or when conducting lender oversight activities and the delegated SBA Lender bears the risk of an incorrect determination.

ii) For 504 loans: The SBA Lender approving a loan under its delegated authority must submit the documents to franchise@sba.gov for a final determination by SBA. SBA Lender must provide contact information for the franchisor/licensor (name and email address only). After receiving SBA's final determination, the delegated SBA Lender may proceed with approving the loan under its delegated authority.

iii. When an Applicant operates under multiple brands, the SBA Lender must enter the name of the franchise and the SBA Franchise Identifier Code for the brand that generates the largest amount of the Applicant's revenue when entering the application or request for an SBA loan number in the SBA Loan System. The SBA Lender must identify all other brands and their SBA Franchise Identifier Codes (if applicable) in the SBA Lender's credit memorandum.

a) For non-delegated loans, the SBA loan processing center will confirm that all of the Applicant's brands are eligible for SBA financial assistance.

b) For delegated loans, the delegated SBA Lender must document in its file that all of the Applicant's brands are eligible for SBA financial assistance.

*iv.* The SBA Lender must obtain a copy of the executed franchise agreement and any other document the franchisor requires the franchisee to sign. (While it is prudent for the SBA Lender to review the Franchise Disclosure Document, as it contains financial information on the franchise brand, it is not necessary for the SBA Lender to retain a copy in its file.)

a) For 7(a) loans, the SBA Lender must obtain these documents prior to any disbursement of loan proceeds.

b) For 504 loans:

i) For all 504 loans, prior to closing, the CDC must obtain a copy of the executed franchise agreement and any other document the franchisor requires the franchisee to sign. The CDC must submit this documentation to their closing counsel, who will review and certify that the franchise documents are executed properly and comply with the SBA procedures set forth in SOP 50 10 8.1 and the SBA Franchise Directory.

ii) CDC Closing Counsel will certify to the legal sufficiency of the franchise documents using the revised Opinion of CDC Counsel when submitting the closing package to the local District Counsel. SBA Form 2268 (504 Debenture Closing Checklist) has the requirement to include the Opinion of CDC Counsel as a requirement (Appendix D to the 504 Authorization Boilerplate).

c) In order to ensure the SBA Lender obtained the required documents and the documents were properly executed, SBA may review these documents when conducting SBA Lender oversight activities, and they must be provided with any request for SBA to honor the guaranty on a defaulted 7(a) loan.

g. Applications involving an applicant franchisor:

The franchisor's brand must be listed on the Directory as an approved brand even if the franchisor will not be executing a franchise agreement in connection with the loan transaction. The franchisor in its own capacity must also meet SBA's Size Standards (the franchisor does not need to be combined with franchisees for determining size).

h. Applications involving Franchise Development Agreements or Area Development Rights:

Franchise Development Agreements (also known as a "Master Franchise Agreements") provide the developer with a geographic area with which to establish additional franchise units. These additional franchise units are owned and operated by other franchisees, and the developer's income is derived from the royalty payments from each franchisee in the developer's geographic territory. Based on those features, these agreements have been determined to be passive and, therefore, an Applicant that is or will be operating under a Franchise Development Agreement is not eligible for SBA financial assistance.

If an Applicant franchisee has an affiliate that operates under an ineligible Franchise Development Agreement, the Applicant franchisee may be eligible for SBA financial assistance, provided that the Applicant and its affiliates are small, and no SBA loan proceeds are used for the benefit of the ineligible affiliate franchise developer.

An Applicant franchisee that is or will be operating under a franchise agreement that provides the franchisee with the right to develop additional units that the franchisee or its affiliates own and operate within its territory ("area development rights" or "Multi-Unit Franchise Agreement"), however, may be eligible provided that the Applicant and its affiliate franchise units are small.

i. Franchise Applicants with Management Agreements:

i. If the Applicant will be using a management agreement that is not part of the franchise disclosure documents, the SBA Lender, not SBA, must review the management agreement or other similar agreements to determine whether the agreement makes the Applicant an ineligible passive business.

ii. Management agreements that give the management company sole discretion over the business operations create ineligible passive businesses. However, if the management company does not have sole discretion to manage the operations of the business and the Applicant exercises meaningful oversight of the business, the Applicant is eligible.

iii. "Meaningful oversight" by the Applicant means involvement in the decisions made concerning the operation of the business, which include a management agreement that provides for the Applicant to do all of the following:

a) Approve the annual operating budget;

b) Approve any capital expenditures or operating expenses over a significant dollar threshold;

c) Have control over the bank accounts; and

d) Have oversight over the employees operating the business (who must be employees of the Applicant).

iv. If the Applicant franchisee is operating under a management agreement where the management company is, or is affiliated with, the franchisor, the Applicant is not eligible. Such a relationship does not result in the franchisee operating as an independent small business.

*v.* See Paragraph E.3, Passive Businesses, above for guidance on passive businesses.

j. Questions on SBA's Franchise Policy, Requests for Reconsideration and Appeals:

i. Questions on SBA's Franchise Policy should be directed to franchise@sba.gov.

ii. Franchisors that would like to appeal SBA's decision not to place them on the Directory may do so by forwarding a copy of the decision, along with an explanation of how the determination is perceived to be inconsistent with SBA Loan Program Requirements, to franchise@sba.gov. Franchise appeals will be reviewed by the SBA Franchise Committee.

iii. There is no right of appeal for final Agency decisions made by the Associate General Counsel for Litigation.

iv. Franchisors that would like to request reconsideration of SBA's determination that they meet the FTC definition of a franchise or that their agreement creates an ineligible passive business may do so by forwarding a copy of the decision, along with an explanation of why that decision is perceived to be incorrect, as well as any supporting documentation to franchise@sba.gov.

## H. CREDIT NOT AVAILABLE ELSEWHERE

(15 U.S.C. 636(a)(1)(A) and 13 CFR § 120.101)

1. The SBA Lender must certify and indicate that the Applicant does not have the ability to obtain some or all of the requested loan funds on reasonable terms from non-Federal, non-State, or non-local government sources, including from the SBA Lender or Third Party Lender, without SBA assistance. If the Applicant's cash flow and collateral, including the adequacy of any third party guaranty, would cause the Applicant's loan to meet conventional credit standards of the SBA Lender or Third Party Lender, the Project is not eligible for an SBA Loan. Failure of the SBA Lender to adequately address the Applicant's need for the desired credit in the credit memorandum may result in SBA declining the application submitted under non-delegated processing or denying liability on the guaranty if the application is approved by a 7(a) Lender under its delegated

authority or, in 504, the pursuit of a CDC Recovery Claim under 13 CFR § 120.938 in the case of fraud, negligence, or misrepresentation by the CDC.

2. The SBA Lender must include in its credit memorandum:
    a. A determination that some or all of the loan is not available from any of the following sources:
        i. The liquidity of owners of 20% or more of the equity of the Applicant, their spouses and minor children, and the Applicant itself (except that SBA permits owners to have reasonable funds set aside for possible future medical expenses, educational expenses (including for the children of the business owner) and retirement needs; and for the Applicant, SBA permits the Applicant to have reasonable funds for capital expenses for the next 24 months and for working capital); or
        ii. Conventional lenders or other non-Federal, non-State, or non-local government sources of credit including the SBA Lender, and for 504 loans, the Third Party Lender. Note: This includes any commitment by a third party to provide financial assistance to the Applicant in the event of a delinquency or default on a payment (e.g., a commitment by a franchisor or licensor to provide financial assistance to the franchisee or licensee).
    b. Substantiate that credit is not available elsewhere by discussing acceptable factors that demonstrate an identifiable weakness in the credit. The SBA Lender must include in its credit memorandum the specific reasons why the Applicant does not meet conventional loan policy requirements, along with relevant supporting documentation. The SBA Lender may not cite the Applicant's inability to meet the SBA Lender's or Third Party Lender's conventional credit score policy as the sole reason that credit is not available elsewhere.

        Acceptable factors that demonstrate an identifiable weakness in the credit or exceed policy limits of the SBA Lender or the Third Party Lender include, among others:

        i. The business needs a longer maturity than the SBA Lender's/Third Party Lender's policy permits to reasonably assure the ability of the loan applicant to repay the debt from the actual or projected cash flow of the business (for example, the business needs a loan that is not on a demand basis);
        ii. The requested loan exceeds the SBA Lender's/Third Party Lender's policy limit regarding the amount that it can lend to one customer;
        iii. The collateral does not meet the SBA Lender's/Third Party Lender's policy requirements;
        iv. The SBA Lender's/Third Party Lender's policy normally does not allow loans to new businesses (e.g., a business that has been in operation for a

period of not more than 2 years) or businesses in the Applicant's industry; and/or

v. Any other factors relating to the particular credit that, by applying prudent lending standards, in the SBA Lender's/Third Party Lender's opinion, cannot be overcome except for the guaranty. These other factors must be specifically explained in the SBA Lender's credit memorandum, and relevant supporting documentation must be included in the loan file. Examples of "other factors" may include business and personal credit history, management experience, leverage ratio, global cash flow, and loan size relative to the age of the business.

3. The SBA Lender/Third Party Lender may not rely on the following factors as the sole basis to demonstrate that the Applicant does not have credit available elsewhere:

   a. For 7(a) loans, the fact that the liquidity of the SBA Lender depends upon the guaranteed portion of the loan being sold on the secondary market; or

   b. SBA's participation will allow the SBA Lender/Third Party Lender to exceed its legal lending limit.

4. The SBA Lender may not rely in any manner on the following factors to demonstrate that the Applicant does not have credit available elsewhere:

   a. The maintenance or improvement of the SBA Lender's/Third Party Lender's rating or performance evaluation under the Community Reinvestment Act (CRA) or its implementing regulations; or

   b. The improvement of the SBA Lender's/Third Party Lender's collateral lien position.

## I. CUSTOMER IDENTIFICATION PROGRAMS

1. SBA requires all participating SBA Lenders, including SBLCs, to comply with the U.S. Department of the Treasury regulations for Customer Identification Programs (CIP) for banks, savings associations, credit unions, and certain non-federally-regulated banks found at 31 CFR § 1020.220.

2. For 504 loans: SBA does not expect CDCs to duplicate the procedures of the Third Party Lender if the Third Party Lender is regulated by a Federal functional regulator (as defined in 31 CFR § 1010.100(r)) and submits annual certifications to the CDC that it (the Third Party Lender or its agent) will comply with the CIP requirements of 31 CFR § 1020.220 with respect to all third party financings of 504 loans. Under these circumstances, it is acceptable to SBA if a CDC's CIP states that the CDC will rely on the Third Party Lender to verify the identity of the SBA Applicant. The CDC has the option of performing its own verification of the identity of the SBA Applicant even if a Third Party Lender has already complied with 31 CFR § 1020.220. If the Third Party Lender has not submitted

the requisite annual certification to the CDC, the CDC must perform its own verification of identity.

## J. OFAC SANCTIONS LIST

1. SBA requires all participating SBA Lenders, including SBLCs, to comply with the U.S. Department of the Treasury regulations for Department of Treasury Office of Foreign Assets Control (OFAC) sanctions lists. SBA Lenders must determine that the applicant business and owners are not listed on the OFAC sanctions lists at the time of application.
2. For 504 loans: SBA does not expect CDCs to duplicate the procedures of the Third Party Lender if the Third Party Lender is regulated by a Federal functional regulator (as defined in 31 CFR § 1010.100(r)) and submits annual certifications to the CDC that it (the Third Party Lender or its agent) will comply with the OFAC requirements with respect to all third party financings of 504 loans. Under these circumstances, it is acceptable to SBA if a CDC's loan policy states that the CDC will rely on the Third Party Lender to verify the SBA Applicant against the OFAC sanctions list. The CDC has the option of performing its own verification of the SBA Applicant even if a Third Party Lender has already complied with OFAC regulations. If the Third Party Lender has not submitted the requisite annual certification to the CDC, the CDC must perform its own search of the OFAC sanctions lists.

# CHAPTER 2: SPECIAL TRANSACTION STRUCTURES

## A. ELIGIBLE PASSIVE COMPANIES

13 CFR § 120.111

The Eligible Passive Company (EPC) Rule is an exception to SBA regulations that prohibit financing assets that are held for their passive income. (13 CFR § 120.130(d)) Because the EPC rule is an exception, the EPC and the OC must comply with all of the conditions in 13 CFR § 120.111 and each condition is interpreted strictly. If all conditions are not complied with, in the event of default on a 7(a) loan, SBA may deny liability on the guaranty. In 504, SBA may pursue a CDC Recovery Claim under 13 CFR § 120.938 in the case of fraud, negligence, or misrepresentation by the CDC.

An Eligible Passive Company (EPC) must use loan proceeds only to acquire or lease, and/or improve or renovate, real or personal property (including eligible refinancing), that it leases to one or more Operating Companies (OCs) for conducting the OC's business, or to finance a change of ownership between the existing owners of the EPC. An EPC may only use loan proceeds to finance a change of ownership between existing owners of the EPC when the real estate or personal property has been held by the selling owner(s) for at least 36 months.

For specific information on change of ownership loans with an EPC/OC structure:

- For 7(a), see Appendix 15: 7(a) Changes of Ownership, and the eligible uses of proceeds section of each delivery method chapter. Note, change of ownership is not an eligible use of proceeds for the CAPLines and EWCP delivery methods, or for revolving facilities.
- For 504, see Section C, Ch. 1, Para. C.13, Change of Ownership for the circumstances under which change of ownership is permitted. Note: See Para. C.13.a.iii. of such Section for important restrictions that apply if using a 504 loan to finance a change of ownership between existing owners of the EPC.

With the exception of a change of ownership between existing owners of the EPC, an EPC may not use loan proceeds to acquire a business, acquire stock in a business or any intangible assets of a business, or to refinance debt that was incurred for those purposes.

In addition, when the EPC and OC(s) are Co-Borrowers:

- A 7(a) loan may include loan proceeds for working capital and/or the purchase of other assets, including intangible assets for the OC’s use; and
- A 504 loan may include loan proceeds for the purchase of fixed assets to be owned by the OC(s).

An EPC can take any legal form or ownership structure (e.g., corporation, partnership, LLC, sole proprietor, tenancy in common, etc.)

A tenancy in common is a form of legal ownership and does not create a new or separate legal entity. There may be several individuals or entities in a tenancy in common, but the tenancy in common is considered one EPC. The loan documents must be signed by all of the members of the tenancy in common.

Multiple OCs that are separately owned can participate in an EPC/OC structure, however, multiple EPCs in one transaction are not permitted. An EPC may own several unique properties that it leases to the same OC(s); however, in the case of multiple OCs, the same OCs (with the same ownership structure) must jointly occupy each property (i.e., it is not permissible for one OC to occupy one property and a different OC to occupy a different property).

1. Conditions that apply to all EPCs:
    a. The OC(s) must be an eligible small business;
    b. The proposed use of proceeds must be an eligible use as if the OC(s) were obtaining the financing directly;
    c. The EPC (with the exception of a trust) and the OC(s) each must be small under the appropriate size standard of 13 CFR Part 121;
    d. The EPC must lease the project property directly to the OC(s); and
        i. Obtain a fully executed written lease;
        ii. The lease must be subordinated to the SBA's mortgage, trust deed lien, or security interest on the property (Note: This is not the same as a Landlord's Waiver);
        iii. The lease must have a term, including options to renew exercisable solely by the OC(s), at least equal to the term of the loan;
        iv. The EPC (as landlord) must furnish as collateral for the loan an assignment of all rents paid under the lease. An assignment of the lease is only required when necessary to perfect the assignment of rents under applicable law, or to enable the SBA Lender to exercise the tenant's rights upon default;
        v. The rent or lease payments cannot exceed the amount necessary to make the loan payment to the Lender and an additional amount to cover the EPC's direct expenses of holding the property, such as routine maintenance, utility expenses, insurance, and property taxes.
        vi. For 504 loans, loan payments to the SBA, the Third Party Lender, and if applicable, to a lender authorized by SBA to provide the Borrower's contribution, are included in the calculation of "loan payment to the Lender." Rent or lease payments cannot include amounts for accelerated payments on the Third Party Loan;
        vii. When calculating repayment ability, the SBA Lender must consider whether

the OC's cash flow will be sufficient to cover the loan payment (for 504 loans, including the loan payment to the Third Party Lender), in addition to the expenses of holding the property including the payment of routine maintenance, property taxes, utility expenses, insurance, and all other ongoing expenses;

viii. The OC(s) must lease 100% of the property from the EPC, but it can sublease a portion of the property under the rules governing occupancy requirements with which all SBA Borrowers must comply (see Ch. 3, Para. C, Occupancy and Leasing Requirements of this Section for more information);

ix. If, in acquiring the property, the EPC becomes the beneficiary or owner of the rights to an existing mineral lease on the property, the EPC must assign its interest in the lease (together with its rights to all rental, mineral, royalty, bonus, or similar lease payments that might accrue by virtue of the existing mineral (oil and gas) lease) to the OC(s); and any such assignment must be subordinated to all Deeds of Trust or Mortgages. In addition, the SBA Lender must take the following actions if applicable:

a) If subordination is not possible:

i) For 7(a) loans: The 7(a) Lender must obtain a legal opinion to that effect;

ii) For 504 loans: CDC Closing Counsel must provide a legal opinion to that effect;

b) If the mineral lease has been terminated, the SBA Lender should attempt to have it removed from the Title Policy;

c) If the SBA Lender is unable to have the mineral lease removed from the Title Policy:

i) For 7(a) loans:

(a) The SBA Lender must provide supporting documentation evidencing the proper assignment of the lease to the OC(s) and obtain a title endorsement to protect SBA's interest in the real property (see, for example, California Land Title Association (CLTA) 100.23 or 100.24).

(b) SBA Lenders processing loans under non-delegated procedures must submit a copy of the lease agreement between the EPC and OC(s) with the application for loan guaranty to SBA. SBA Lenders processing loans under delegated authority must keep a copy of the executed lease in their loan file and must submit the lease with any request to SBA to purchase the guaranty.

ii) For 504 loans: The CDC Closing Counsel must include language in the Opinion of Counsel indicating that they have examined and relied upon the accuracy of the assignment document and obtain a title endorsement to protect SBA's interest in the real property (see, for example, California Land Title Association (CLTA) 100.23 or 100.24).

e. An EPC (excluding a trust) may not engage in any business activity other than leasing the property to the OC(s). The EPC may own more than one property provided all the property is leased to the same OC(s).

f. The OC(s) must be a guarantor or a Co-Borrower on the loan.

i. Each holder of an ownership interest constituting at least 20% of either the EPC or the OC(s) must guarantee the loan (if the holder is a trust, then the Trustee shall execute the guarantee on behalf of the trust).

ii. Each spouse owning less than 20% of an EPC or OC must personally guarantee the loan in full when the combined ownership interest of both spouses and minor children is 20% or more.

iii. For a non-owner spouse, the SBA Lender must require the signature of the spouse on the appropriate collateral documents. The spouse's guaranty secured by jointly held collateral will be limited to the spouse's interest in the collateral.

iv. If a person has executed the Note as a Borrower in an individual capacity, that person does not also have to execute a personal guaranty.

v. When deemed necessary for credit or other reasons, SBA or, for a loan processed under an SBA Lender's delegated authority, the SBA Lender, may require other appropriate individuals or entities to provide full or limited guaranties of the loan without regard to the percentage of their ownership interests, if any.

vi. The OC(s) must be a Co-Borrower if it receives any proceeds or if proceeds will be used to purchase any assets for the OC(s) use.

g. The amount of any loan received by an EPC applies to the loan limit of both the EPC and the OC.

2. Conditions that apply when the EPC is owned in whole or in part by a trust.

a. The eligibility status of the Trustor will determine trust eligibility.

b. All donors to the trust will be deemed to have Trustor status for eligibility purposes.

c. The Trustee must warrant and certify that the trust will not be revoked or substantially amended for the term of the loan without the prior written consent of SBA.

d. The Trustor must personally guarantee the loan.

   i. If an Employee Stock Ownership Plan trust agreement prohibits it from being a guarantor or Co-Borrower, then it cannot use the EPC form of borrowing.

   ii. Beneficiaries that exercise any control over the actions of the trust also must guarantee the loan.

e. The Trustee shall certify in writing to SBA, or to the SBA Lender processing a loan under its delegated authority, that:

   i. The Trustee has authority to act;

   ii. The trust has authority to borrow funds, pledge trust assets, and lease the property to the OC(s);

   iii. The Trustee has provided accurate, pertinent language from the trust agreement confirming the above; and

   iv. The Trustee has provided SBA or the SBA Lender processing a loan under its delegated authority with a true and complete list of all trustors and donors and will provide an updated list to SBA or the SBA Lender processing a loan under its delegated authority any time the list changes.

f. The trust itself does not have to be small by SBA size standards.

3. Size Determinations under the EPC rule.

   a. If the EPC and the OC(s) are affiliated, the two companies are combined for determining size.

      i. If there is only one OC, use the OC's NAICS code.

      ii. If there are multiple, unaffiliated OCs, use the NAICS code of the OC that generates the most revenue. Note: Each OC must be small based on its own NAICS code.

      iii. If the multiple OCs are affiliated, then use the rules detailed in 13 CFR § 121.107 for determining the primary industry of affiliated businesses. The NAICS Code of the primary industry of the OC shall be the identifying NAICS Code.

   b. If the EPC and the OC(s) are not affiliated, each entity must be small under the size requirement for its particular industry.

      The existence of a lease between the EPC and the OC(s) does not, in and of itself, create an affiliation, even if the EPC and OC(s) are Co-Borrowers.

4. When sending data to SBA, use the same NAICS Code that was used to determine size for the Applicant.

5. Submission of Financial Statements by the EPC and the OC(s):

a. The EPC and each OC must submit Financial Statements. The OC's statements are subject to tax verification.

b. The regular requirement for an Aging of receivables and payables is waived for EPCs.

## B. LOANS TO EMPLOYEE STOCK OWNERSHIP PLANS (ESOPS)

For 7(a) loans only: SBA may assist a qualified employee trust (or equivalent trust) that meets the requirements and conditions for an ESOP prescribed in all applicable IRS, Treasury, and Department of Labor regulations. 13 CFR §§ 120.350 - 120.354 The Lender must confirm that the ESOP meets the requirements and conditions prescribed by other regulatory bodies. SBA will not review any applications, even those submitted via non-delegated processing, for compliance with the requirements imposed by other regulatory bodies for these types of transactions.

1. SBA may guarantee a 7(a) loan to an ESOP for two purposes:
   a. Purchasing a controlling interest (at least 51 percent) in the employer small business; or
   b. Purchasing qualified employer securities. The employer small business may use the funds received from the purchase of the qualified employer securities for any general 7(a) purpose.
   c. In the case of either a. or b. above, the small business concern must be a Co-Borrower on the 7(a) loan.
2. SBA may guarantee a 7(a) loan to an eligible employer small business for the sole purpose of making a loan to a qualified employee trust (ESOP) that results in the qualified employee trust owning at least 51 percent of the employer small business concern.
3. Transaction costs associated with the purchase of the controlling interest by the ESOP or equivalent trust may be included in the use of proceeds, but any transaction costs associated with setting up the ESOP may not be included in the use of proceeds.
4. If the seller of the employer small business remains as a partial owner, the seller must provide a full, unlimited guarantee regardless of percentage of ownership. Note: This is a statutory requirement and cannot be waived.
5. Lenders may process loans to an ESOP or to an eligible small business owned or controlled by an ESOP under delegated authority. However, Lenders are reminded that regardless of processing method (delegated or non-delegated) the ESOP must be in compliance with IRS, Treasury, and the Department of Labor requirements.
6. The IRS prohibits ESOPs from guaranteeing a loan; therefore, SBA does not require the ESOP to guarantee the loan. In addition, members of the ESOP are not required to personally guarantee the loan. All owners of the Applicant who hold an ownership

interest in the small business outside the ESOP are subject to SBA's guaranty requirements. (See Ch. 5, Para. A, Guaranties, of this Section for more information.)

7. The application cannot be structured as an EPC/OC. (13 CFR § 120.111(a)(6)) SBA regulations require each 20% or more owner of the EPC and each 20% or more owner of the OC to guarantee the loan, and the regulation does not provide for an exception.
8. Prior to first disbursement, the Lender must obtain documentation that the ESOP or equivalent trust meets the requirements of all applicable IRS, Treasury, and Department of Labor regulations. Whether processed under delegated or non-delegated procedures, the SBA Lender must determine whether the applicant and ESOP plan meet legal requirements and the requirements and conditions prescribed by other regulatory bodies.
9. Loans to ESOPs for the purpose of purchasing a controlling interest (at least 51 percent) in the employer small business are not subject to the requirement for equity injection.
10. When an SBA loan is used to purchase a business owned by an ESOP resulting in a change of ownership where the ESOP is being dissolved, the employees (owners of the ESOP), except for illegal aliens, may remain as employees of the business despite other provisions in this SOP to the contrary.
11. Regardless of the requirements stated throughout this SOP for business valuations, an independent business valuation is not required when the Lender is making a loan involving ESOPs for the types of loans discussed in this Paragraph B. In lieu of an independent business valuation, the Lender may use the valuation obtained by the ESOP that was made in accordance with ERISA specifications.

## C. COOPERATIVES

1. Eligibility: All Applicants operating under a cooperative structure must meet SBA's eligibility requirements.
2. SBA Lenders may process loans to a cooperative or to an eligible small business owned or controlled by a cooperative under delegated authority.
3. Each loan must be guaranteed by at least one individual or entity. (See Ch. 5, Para. A, Guaranties, of this Section for more information.)
4. For 7(a) only: SBA may guarantee a loan to a cooperative to purchase a controlling interest (51% or more) in the employer small business. Any transaction costs associated with the purchase of the controlling interest, but not costs associated with setting up the cooperative, may be included in the use of proceeds.
5. The SBA Lender must submit supporting organizational documents and agreements as applicable with the loan application depending on the type of cooperative and the purpose of the loan (e.g., a loan to a cooperative to acquire a controlling interest in the employer concern), which may include Cooperative Agreement; Organization documents; Articles

of Incorporation/Organization; Bylaws; Operating/Conversion/Redemption/Membership Agreement(s); or any other agreements as necessary.

6. Whether processed under delegated or non-delegated procedures, the SBA Lender must confirm that the applicant and cooperative meet legal requirements and the requirements and conditions prescribed by other regulatory bodies. SBA will not review any applications, even those submitted via non-delegated processing, for compliance with the requirements imposed by other regulatory bodies for these types of transactions.

## D. 401(K) PLANS INCLUDING ROLLOVERS AS BUSINESS START-UPS (ROBS) PLANS

A business that is owned in whole or in part by a 401(k) plan (including a Rollovers as Business Startups (ROBS) plan) may be eligible provided the SBA Lender complies with the requirements in this section and the plan complies with all applicable IRS, Treasury, and Department of Labor requirements.

When evaluating applications involving such businesses, SBA Lenders must consider that a 401(k) plan sponsor's failure to administer the plan properly may result in plan disqualification and adverse tax consequences to the plan's sponsor and its participants, which may impact the Borrower's ability to repay the loan.

The SBA Lender must confirm that the ROBS Plan meets the requirements and conditions prescribed by other regulatory bodies. SBA will not review any applications, even those submitted via non-delegated processing, for compliance with the requirements imposed by other regulatory bodies for these types of transactions.

Applications where the Applicant or any owner (including a corporation formed through a ROBS plan) is a:

- Single Employer Plan, including ROBS plans, may be processed under an SBA Lender's delegated authority. Note: Any subsequent contributions required under IRS and/or Employee Retirement Income Security Act (ERISA) regulations are permitted.
- Multiple-Employer Plan, (i.e., plans that hold in trust the assets of other businesses), including ROBS plans, may be processed under an SBA Lender's delegated authority. NOTE: Size standards and maximum SBA guarantee limits to a Borrower and its affiliates apply to the multiple-employer plan.

1. The SBA Lender must:
    a. Identify in the SBA Loan System and in the credit memorandum:
        i. The specific type of 401(k) plan (Single Employer Plan, Multiple Employer Plan, etc.); and
        ii. If applicable, that the Applicant is using a ROBS plan for the equity contribution or other purpose (if the latter, specify the purpose of the ROBS plan).

b. Obtain the full unconditional guaranty of the sponsor(s) of the 401(k) plan regardless of the sponsor's individual ownership interest in the Applicant concern. This guaranty must be a secured guaranty if required by SBA's existing collateral policies. For more information on collateral: For 7(a), see Appendix 19. For 504, see Section C, Ch. 1, Para. E.2.a., Collateral.

c. The SBA Lender must obtain the following 401(k) plan documentation with the loan application:

i. A favorable determination letter from IRS providing advance assurance that the terms of the 401(k) plan satisfies qualification requirements. IRS Publication 794 explains the significance of the favorable determination letter, points out critical areas that may affect the qualified status of a 401(k) plan, and provides general information on the reporting requirements for the 401(k) plan;

ii. For an existing 401(k) plan, the Annual Return/Report of Employee Benefit Plan (e.g., IRS Form 5500, IRS Form 5500-EZ, etc.);

iii. For a ROBS plan:

a) C Corporation formation documents;

b) 401(k) plan adoption documents;

c) Stock purchase documents; and

d) Related corporate resolutions.

2. SBA loan proceeds may not be used for any 401(k) plan formation costs.

3. The application cannot be structured as an EPC/OC. (13 CFR § 120.111(a)(6)) Under IRS regulations, the 401(k) cannot guaranty the loan. SBA regulations require each 20% or more owner of the EPC and each 20% or more owner of the OC to guarantee the loan, and the regulation does not provide for an exception.

4. Prior to any disbursement of loan proceeds, the SBA Lender must obtain the Borrower's certification that the Borrower and the 401(k) plan are in compliance with all applicable IRS, Treasury, and Department of Labor requirements and that it will comply with all relevant operating and reporting requirements. Whether processed under delegated or non-delegated procedures, the SBA Lender must determine whether the applicant and proposed structure meet legal requirements and the requirements and conditions prescribed by other regulatory bodies for these types of transactions.

# CHAPTER 3: USES OF PROCEEDS

## A. ELIGIBLE USES OF PROCEEDS

13 CFR § 120.120

1. A Borrower may use loan proceeds from any SBA Loan to:
    a. Acquire land (by purchase or lease) as part of an eligible project;
    b. Improve a site (e.g., grading, streets, parking lots, landscaping) including up to 5 percent for community improvements such as curbs and sidewalks;
    c. Purchase one or more existing buildings;
    d. Convert, expand, or renovate one or more existing buildings;
    e. Construct one or more new buildings;
    f. Acquire (by purchase or lease) and install fixed assets (for a 504 loan, these assets must have a useful life of at least 10 years and be at a fixed location, although short-term financing for equipment, furniture, and furnishings may be permitted where essential to and a minor portion of the 504 Project);
    g. Finance a Lender's Other Real Estate Owned (OREO):

        When loan proceeds will be used to finance the purchase of real estate owned by the 7(a) Lender; or for 504, the Third Party Lender, making the loan, the application must:

        i. Include an independent real estate appraisal that meets the SBA Loan Program Requirements (the appraisal requirement cannot be delayed until loan closing). For 7(a), the appraisal must also provide the liquidation value of the real estate.
        ii. Include an explanation of the circumstances surrounding the 7(a) Lender or Third Party Lender's acquisition of the real estate. If the acquisition of the property was triggered by a business failure at that particular location, the SBA Lender must submit a detailed explanation of why the new Applicant will succeed at that same location; and
        iii. For 7(a): Identify the SBA Lender's cost in the real estate. In order to get the full SBA guaranty, the sales price may not exceed the mortgage balance plus care and preservation expenses or the liquidation value, whichever is less. If the sales price is greater than the mortgage balance plus care and preservation expenses or the liquidation value (whichever is less), then the SBA guaranty will be reduced accordingly.

            For example:

OREO Sales Price: $1.2 million

Lender's costs or liquidation value (whichever is less): $1.0 million

Guaranty amount: 75% of $1.0 million: $750,000

Effective SBA guaranty: $750,000/$1,200,000: 62.5%

2. For 7(a) only, Borrower may also use loan proceeds for:
    a. Inventory;
    b. Supplies;
    c. Raw materials (including work-in-progress);
    d. Working capital to finance everyday operations and short-term operational needs.
        i. Working capital may be used to acquire and/or use business software or cloud computing services. Examples may include facilitating business operations, product or service delivery, the processing, payment, or tracking of payroll expenses, human resources, sales and billing functions, or accounting or tracking of supplies, inventory, records and expenses;
        ii. If the Operating Company is a Co-Borrower with the Eligible Passive Company, part of the loan proceeds may be applied for working capital and/or the purchase of other assets, including intangible assets, for use by the Operating Company.
        iii. Working capital proceeds may not be used to refinance existing debt or to finance any ineligible purpose.
    e. Revolving lines of credit under CAPLines, SBA Express, Export Express, and the Export Working Capital Program (EWCP);
    f. Under CAPLines, Export Express or EWCP: For Standby Letter of Credit when required as a bid bond, performance bond, or advance payment guarantee.
3. Farm Enterprises
    a. The purchase of land, buildings, and land improvements (fencing, irrigation systems, construction of dikes, silos, barns, hog and dairy facilities, etc.) as part of an eligible project;
    b. Construction, renovation, or improvement (including water systems) of farm buildings other than residences;
    c. For 7(a) only:
        i. The purchase of farm machinery and equipment;
        ii. The purchase of seed and the acquisition of animals;

iii. Operating expenses directly related to the farming operation, excluding personal or family living expenses; and

d. The refinancing of debt related to the farming operation, excluding personal or family debt, provided the refinancing meets SBA Loan Program Requirements.

Note: The acquisition of land in excess of the farming operation's needs is not an eligible use of proceeds. In addition, the Applicant must not use loan proceeds to purchase vacant or row crop land for possible future use, future construction, or to lease to third parties. For example, a concentrated animal feedlot operation (CAFO) that only requires 10 acres of land for its operation (including housing and feeding of the animals, service and access roads, and waste management facilities) may not use SBA-guaranteed loan proceeds to obtain excess farmland that is not used in the operation of the Applicant. If excess land is being acquired at the same time as the SBA Loan, the excess land must be financed from sources other than SBA and the source of the financing must be documented in the loan file.

## B. RESTRICTIONS ON USES OF PROCEEDS

13 CFR § 120.130

Loan proceeds may not be used for any of the following purposes (including the replacement of funds used or borrowed for any such purpose):

1. Payments, distributions, or loans to an Associate of the Applicant (as defined in 13 CFR § 120.10), except for compensation for services actually rendered at a fair and reasonable rate or to facilitate 7(a) loans for changes of ownership in accordance with 13 CFR § 120.202 and the guidance in Section B of this SOP on partial changes of ownership;
2. Refinancing a debt owed to a Small Business Investment Company (SBIC) or a New Markets Venture Capital Company (NMVCC);
3. Floor plan financing;
4. Revolving lines of credit, except under SBA Express, CAPLines, Export Working Capital Program (EWCP), Manufacturers' Access to Revolving Credit (MARC), and Export Express programs;
5. Investments in real or personal property acquired and held primarily for future development, sale, lease, or investment (except for a loan to an Eligible Passive Company or to a small contractor under the Builders CAPLine program). The purchase of excess land (land that is not for immediate use as part of the project) is not eligible to be funded by SBA loan proceeds;
6. Payment of Delinquent Taxes;
    a. Loan proceeds must not be used to pay past-due Federal, state, or local payroll taxes, sales taxes, or similar taxes that are required to be collected by the Applicant

and held in trust on behalf of a Federal, state, or local government entity (13 CFR § 120.130(e)).

b. Payment only for delinquent business income taxes may be permitted if the Applicant has an approved payment arrangement with the IRS and the Applicant is current on the payments in the arrangement.

7. 13 CFR § 120.881 For the 504 Loan Program only: To finance the relocation of the Applicant out of a community, if there will be a net reduction of one-third or more in the Applicant's workforce or a substantial increase in unemployment in any area of the country. An exception may be allowed if the CDC can justify the relocation because:

   a. The relocation is for key economic reasons and crucial to the continued existence, economic well-being, and/or competitiveness of the Applicant; and

   b. The economic development benefits to the Applicant and the receiving community outweigh the negative impact on the community from which the Applicant is moving.

8. To pay any creditor in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from an existing debt 13 CFR § 120.201 and 13 CFR § 120.884(b).

9. A purpose that does not benefit the small business, including a loan to an Applicant for the benefit of an affiliated business;

10. Whether at loan origination or as a servicing action, SBA Lenders may not permit a C-PACE loan to be made on a property that has or will have a 7(a) or 504 loan.

11. Any use restricted by 13 CFR §§ 120.201 and 120.884 (specific to 7(a) loans and 504 loans respectively).

## C. OCCUPANCY AND LEASING REQUIREMENTS

1. Occupancy

   13 CFR § 120.131

   Amount of Rentable Property (based on the total project) that can be leased:

   a. When loan proceeds are used to purchase or improve real estate, or when debt secured by real estate is refinanced with loan proceeds:

      i. For an existing building, the Applicant must occupy 51% of the Rentable Property and may lease to a third party up to 49%; or

      ii. For new construction, the Applicant must occupy 60% of the Rentable Property, may permanently lease to a third party up to 20% and temporarily lease an additional 20% with the intention of using some of the additional 20% within 3 years and all of it within 10 years.

   b. When the real estate is owned by an EPC:

i. The EPC must lease 100% of the Rentable Property to an eligible OC(s).

ii. For an existing building, the OC(s) must occupy 51% of the Rentable Property and may sublease up to 49%; or

iii. For new construction, the OC(s) must occupy 60% of the Rentable Property, may permanently sublease to a third party up to 20% and temporarily sublease an additional 20% with the intention of using some of the additional 20% within 3 years and all of it within 10 years.

c. "Rentable Property" is the total square footage of all buildings or facilities used for business operations (13 CFR § 120.10) excluding stairways, elevators, and mechanical areas and including common areas. Rentable Property may also include exterior space (except parking areas) that is actively used in Borrower's business operations. Examples of exterior space that is actively used in Borrower's business operations include: outdoor storage yards for general contractors, trucking companies, and moving and storage companies; or boat slips and docks for marinas. To determine the occupancy percentage allocated to the Applicant or OC(s), the SBA Lender may include the square footage of all common areas. In an existing building zoned for both commercial and residential use, subject to the space occupancy requirements set forth above, the business owner may either occupy or rent to a third party the space zoned for residential use. However, any residential property occupied by the business owner will only be considered to be occupied by the business if it meets the requirements of Subparagraph h below as well as zoning requirements.

d. Circumstances may justify allowing the Applicant a period of time after closing of the SBA Loan to comply with the above occupancy requirements such as when a pre-existing lease may have a few more months to run. In no case may the small business have more than 1 year to meet occupancy requirements.

CDCs must not submit a 504 closing package if the Borrower will not be occupying and operating in the required amount of Project property after closing and funding. If the Borrower will not be able to meet the occupancy requirements, the CDC must submit in advance and in writing to SLPC a request to extend the period of time necessary for the Borrower to meet occupancy requirements, along with an explanation and any supporting documentation, for SLPC approval. The underlying premise is that an SBA 504 loan is permanent, take out financing. A CDC must not submit a 504 closing package where the Borrower is not occupying and operating upon funding, unless facts to the contrary have been submitted to and approved by the SLPC in advance. If SLPC approves such request, once the Borrower is occupying the property in accordance with the Authorization, the CDC must submit a 327 action certifying the Borrower's compliance within the approved timeframe.

e. The restrictions above apply regardless of whether the Rentable Property is leased to a commercial or residential tenant.

f. The Borrower may not use loan proceeds to improve or renovate any of the Rentable Property to be subleased to a third party. For 504 loans, such improvements may not secure the Third Party Loan.

g. During the life of the loan, the real estate pledged as collateral for the loan, or where the Borrower or Operating Company conducts its business operations, may not be leased to or occupied by any business that the Borrower or Operating Company knows is engaged in any activity that is illegal under Federal, state or local law or any activity that can reasonably be determined to support or facilitate any activity that is illegal under Federal, state or local law (such as a marijuana dispensary). If a Borrower or Operating Company does lease space to such a business, for 7(a) loans, the Lender must notify SBA counsel as soon as the Lender becomes aware of the lease and advise of the action(s) the Lender intends to take and, for 504 loans, the CDC must notify SBA counsel as soon as the CDC becomes aware of the lease to determine what action(s) should be taken.

h. Residential Space as Part of the Business

If the nature of the business requires a resident owner or manager, loan proceeds may be used for the purchase of an existing building(s) or construction of a new building(s) that includes residential space essential to the business. The square footage of the residential space must be appropriate to the needs of the business and may not exceed 49% of the total property. For example, a horse-boarding facility may require that someone be on premises at all times to care for the horses. In this case, the residential property would be considered to be occupied by the business.

2. Responsibilities When the Borrower is Leasing Space

a. When the Borrower is operating in leased space and $500,000 or 30% of loan proceeds (whichever is less) will be used for leasehold improvements or when $500,000 or 30% of the proposed collateral (whichever is less) consists of leasehold improvements, fixtures, machinery, or equipment that is attached to leased real estate:

i. The SBA Lender must obtain a copy of the written lease between the Borrower and the landlord. For 7(a) loans, the lease term, including renewal options exercisable only by the Borrower, should equal or exceed the term of the loan. For 504 loans, the lease term must equal or exceed the term of the loan. An assignment of lease and Landlord's waiver should be obtained.

ii. If the SBA Lender is unable to obtain the assignment of lease or landlord's waiver, for both 7(a) and 504 loans, the lease term, including renewal options exercisable only by the Borrower, must equal or exceed the term of the loan.

Additionally, the SBA Lender must document in its file its attempt to obtain the assignment and the landlord's waiver and the reason(s) for not obtaining them.

b. If the loan proceeds will finance improvements on a leasehold interest in land, the underlying ground lease must include, at a minimum, detailed clauses addressing the following:

   i. Tenant's right to encumber leasehold estate;

   ii. No modification or cancellation of lease without SBA Lender's or assignee's approval;

   iii. SBA Lender's or assignee's right to:

      a) Acquire the leasehold at foreclosure sale or by assignment and right to reassign the leasehold estate (along with right to exercise any options) by SBA Lender or successors; lessor may not unreasonably withhold, condition, or delay the reassignment;

      b) Sublease;

      c) Share in hazard insurance proceeds resulting from damage to improvements;

      d) Share in condemnation proceeds; and

      e) SBA Lender's or assignee's rights upon default of the tenant or termination.

c. If the loan proceeds will finance improvements made by the Borrower/tenant on a space that the Borrower is leasing, and if the landlord will reimburse the Borrower for such tenant improvements, the landlord reimbursement must be used to pay down the loan to a point that will not trigger a subsidy recoupment fee, and any remaining funds may be used for business working capital or to decrease the rent payments. Alternatively, if the Lender can document that the landlord reimbursement has been factored into the Lender's working capital adequacy analysis, the landlord reimbursement may be used for business working capital or to reduce the rent payments.

d. For loans collateralized by Indian lands held in trust, if the owner of the land cannot get approval for a lien on the property, the SBA Lender may consider requiring an Assignment of Lease. The Assignment of Lease also has to be approved by the Secretary of the Interior or his/her authorized representative.

# CHAPTER 4: ETHICS, FEES, AND AGENTS

13 CFR Parts 103, 105, and 120.

Any person or entity applying for SBA assistance does not need an Agent to conduct business with SBA. The term "Conduct Business with SBA" is defined at 13 CFR § 103.1(b).

## A. ETHICAL REQUIREMENTS

1. Conflicts of Interest:

   Neither an SBA Lender nor its Associates may have a real or apparent conflict of interest with a small business with which it is dealing or SBA (13 CFR § 120.140 and 13 CFR Part 105). SBA Lenders must exercise care and judgment in determining whether a conflict of interest exists and document the file in detail. SBA will not guarantee a loan if the SBA Lender, its Associates, partner(s), or a close relative:

   - Has a direct or indirect financial or other interest in the Applicant; or
   - Had such interest within 6 months prior to the date of application.

   SBA is released from liability on its guaranty, in its discretion, if the SBA Lender, its Associates, partner(s) or a close relative acquires such an interest at any time during the term of the loan.

2. Standards of Conduct Reviews for Applicants

   a. The Standards of Conduct Counselor for the Agency is the Designated Agency Ethics Official. 13 CFR § 105.402(a)

   b. If an Applicant has, as an employee, owner, general partner, managing member, attorney, agent, owner of stock, officer, director, creditor or debtor, an individual who, within 1 year prior to the loan application, was an SBA Employee (as defined by 13 CFR § 105.201(a)), the loan application must be approved by the Standards of Conduct Counselor. 13 CFR § 105.203(a)

   c. If an Applicant has, as its sole proprietor, general partner, managing member, officer, director, or stockholder with a 10% or more interest, an individual who is an SBA Employee (as defined by 13 CFR § 105.201(a)) or a Household Member of an SBA Employee, the loan application must be approved by the Standards of Conduct Committee at SBA Headquarters. (13 CFR § 105.204) A "Household Member" of an SBA Employee includes:

      i. The spouse of the Employee;

      ii. The minor children of the Employee; and

iii. The blood relatives of the Employee, and the blood relatives of the Employee's spouse, who reside in the same place of abode as the Employee. 13 CFR § 105.201(d)

d. If an Applicant has, as its sole proprietor, general partner, managing member, officer, director, or stockholder with a 10% or more interest, or a Household Member of such individual, an individual who is a Member of Congress, an appointed official or employee of the legislative or judicial branch of the Federal Government, a member or employee of a Small Business Advisory Council, or a SCORE volunteer, the loan application must be approved by the Standards of Conduct Committee. 13 CFR §§ 105.301(c) and 105.302(a).

e. When a Standards of Conduct approval is required, the application should be processed by the appropriate processing center and, if appropriate, be conditionally approved and forwarded to the Standards of Conduct Counselor or Standards of Conduct Committee (through the Standards of Conduct Counselor). The Standards of Conduct Counselor will notify the processing center of the final Agency decision, and the processing center will notify the SBA Lender accordingly.

3. Other Government Employees:

a. The Applicant must submit to the SBA Lender a statement of no objection signed by the appropriate **ethics official** of the pertinent department or military service if its sole proprietor, general partner, managing member, officer, director, or stockholder with a 10% or more interest, or a Household Member of such individual, is an employee of another department or agency of the Federal Government (Executive Branch) in a grade of at least GS-13 (or its equivalent). SBA requires a new statement of no objection for each loan.

b. SBA Lenders must submit the statement as a PDF attachment to SNOMemos@sba.gov and receive written clearance from SBA prior to submitting the application to the SBA loan processing center (non-delegated) or processing the application under their delegated authority. SBA Lenders processing a loan under non-delegated procedures must submit a copy of SBA's written clearance with the application to the SBA loan processing center. (13 CFR § 105.301(a)) SBA Lenders processing a loan under delegated procedures must retain SBA's written clearance in the loan file. SBA will review the statements when conducting lender oversight activities and, for 7(a) loans, the statement must be included in any request for SBA to honor its guaranty in the event of default by the Borrower.

## B. DEBARMENT, SUSPENSION, AND EXCLUSION (SAM.GOV/SAFER WEB)

Individuals and entities suspended, debarred, revoked, or otherwise excluded under the SBA or Government-wide debarment regulations are not permitted to conduct business with SBA. See 2 CFR Part 180, adopted by reference in 2 CFR Part 2700 (SBA Debarment Regulations).

SBA Lenders are responsible for consulting the System for Award Management's Exclusions (SAM Exclusions) or any successor system to determine if any of the following have been suspended, debarred, revoked, or otherwise excluded by SBA or another Federal agency. (www.sam.gov/SAM/).

Federal Motor Carrier Safety Administration (FMCSA) requires companies that operate commercial motor vehicles transporting passengers or hauling cargo in interstate commerce to obtain a USDOT number. If the Applicant is required by FMCSA to have a valid USDOT number to operate, in addition to the SAM exclusion search, the Lender must verify the USDOT number in the SAFER Web system (SAFER Web – Company Snapshot).

1. Evidence of the SAM Exclusions search (for example, a screen shot of the search results) for each of the following must be documented in the loan file:
    a. Small business Applicant *and*;
    b. Each of the following:
        i. For a sole proprietorship, the sole proprietor;
        ii. For a partnership, all general partners; limited partners owning 20% or more of the equity of the firm; or any partner that is involved in management of the Applicant business;
        iii. For a corporation, all owners of 20% or more of the corporation, and each officer and director;
        iv. For limited liability companies, all members owning 20% or more of the company; each officer, director, and managing member;
        v. Key Employees;
        vi. Living Trustor (if the Applicant business is owned by a trust);
        vii. The legal entity, when 20% or more ownership interest in the applicant is held by a corporation, partnership, or other form of legal entity; and
        viii. If structured as an EPC/OC, both the EPC and the OC, regardless of whether the OC is a borrower or a guarantor.
2. Evidence of the SAM Exclusions search (for example, a screenshot of the search results) for each of the following must be documented in the SBA Lender's files. The SAM Exclusions search is only required once and must be completed prior to the entity or person's first day of work on SBA-related business.
    a. SBA Lender's employees who are involved in any stage of processing, closing, servicing, or liquidating the SBA loan or have access to the corresponding data;
    b. Agents;
    c. For 7(a), Lender Service Providers (LSP) and LSP employees; and

d. For 504, contractors who are providing services to the CDC under an SBA-approved professional services contract in accordance with 13 CFR § 120.824. See Para E.6.a., Professional Services Contractors, in this Chapter for more information.

3. For companies required by FMCSA to have a USDOT number, the Lender must provide evidence of the SAFER web system (for example, a screenshot of the search results) for the following information:

   a. An Active USDOT number, in good standing; and

   b. A physical address that matches the physical address of the company (no P.O. boxes).

## C. 7(A) LOAN PROGRAM FEES

1. Fees the Lender Pays SBA

   SBA Guaranty Fee (also known as Upfront Fee) and the 7(a) Lender's Annual Service Fee (also known as the SBA On-Going Guaranty Fee). (13 CFR § 120.220) The 7(a) Lender is responsible for payment to SBA of the Upfront Fee and the Lender's Annual Service Fee in order to obtain and maintain the SBA guaranty.

   a. SBA Guaranty Fee (Upfront Fee).

      The Upfront Fee is the fee a 7(a) Lender must pay to SBA for each loan guaranteed under the 7(a) program. The 7(a) Lender is permitted to pass the cost of the Upfront Fee to the Borrower. The Agency automatically calculates the Upfront Fee for each individual loan. This calculation is modified in SBA's loan accounting system and the SBA Loan System to include changes to the fee that are necessary due to other loans approved within the past 90 days. Short-term loans are not included in this calculation. For more information, see below or contact the processing center or Lead District Office.

      The Borrower may use loan proceeds to pay the Upfront Fee; however, the first disbursement may not be made primarily for the purpose of paying the Upfront Fee. If the Borrower plans to use loan proceeds to pay the Upfront Fee, the SBA Terms and Conditions must include a Use of Proceeds category for this purpose. *Note: When an escrow closing is used, the* 7(a) *Lender may charge the Borrower the Upfront Fee only when all loan funds have been disbursed to the Borrower from the escrow account.*

      i. Calculation of the Upfront Fee.

         The total loan amount determines the percentage that is used to calculate this fee. However, the Upfront Fee is based on the guaranteed portion of the loan and not the total loan amount. The chart below describes the applicable fees.

         MAXIMUM UPFRONT FEE CHART (See Note 1)

| Gross Loan Size | Maximum Fees (See Note 1) |
|---|---|
| Loans of $150,000 or less (Maturity more than 12 months) (See Note 2) | 2% of guaranteed portion<br>7(a) Lender is authorized to retain 25% of the fee. |
| $150,001 to $700,000 (Maturity more than 12 months) | 3% of guaranteed portion |
| $700,001 to $5,000,000 (Maturity more than 12 months) (See Note 3) | 3.5% of guaranteed portion up to $1,000,000 PLUS 3.75% of the guaranteed portion over $1,000,000 |
| Short-Term Loans – up to $5 million (Maturity of 12 months or less) | 0.25% of the guaranteed portion |

Note 1: The above table describes the maximum Upfront Fees as authorized by 13 CFR § 120.220. However, SBA may announce temporary changes for a specific fiscal year through an Information Notice.

Note 2: For example, the Upfront Fee on a $100,000 loan with an 85% guaranty would be 2% of $85,000 or $1,700, of which the 7(a) Lender may retain $425.

Note 3: For example, the Upfront Fee on a $5,000,000 loan with a 75% guaranty ($3.75 million guaranteed portion) would be 3.5% of $1,000,000 ($35,000) PLUS 3.75% of $2,750,000 ($103,125), which totals $138,125.

For SBA Express only : The Upfront Fee is waived for loans to businesses owned and controlled by a veteran (other than a veteran who received a Dishonorable or Bad Conduct Discharge), Service-Disabled Veterans; Active Duty military service member participating in the military's Transition Assistance Program (TAP); or spouse of a Veteran, Active Duty service member, or widowed spouse of a service member who died while in service or of a service-connected disability.

ii. Upfront Fee Calculation for Multiple 7(a) Loans Within 90 Days.

a) Except for scenarios involving Working Capital Pilot (WCP) and Export Working Capital Program (EWCP) loans , when two or more 7(a) loans (with maturities exceeding 12 months) are approved for an applicant, including its affiliates, within 90 days of each other, the loans are considered as one loan for the purpose of determining the percentage of guaranty and Upfront Fee calculation, regardless of whether the loans were approved by the same or different Lenders.

b) When two or more 7(a) loans are approved within 90 calendar days of each other, the applicable fee for the subsequent loans is equal to the Upfront Fee that would have been charged had all the loans been combined into one loan. The applicable fee for the subsequent loan(s)

will equal the amount of the fee that would have been charged had the loans been combined, less the amount of the fee from the first loan approved.

For WCP loans, and EWCP loans: When two or more 7(a) loans are approved for an Applicant (including its affiliates), within 90 days of each other, and one or more one of the 7(a) loans is a WCP or EWCP, the loan amounts are combined and treated as if they are one loan to determine the percentage of guaranty and Upfront Fee relief for manufacturers. For purposes of calculating the Upfront Fee in this scenario, WCP and EWCP loans are not combined with any other 7(a) loans since their guaranty fees are based on the maturity.

c) When the Applicant receives both a short and long term 7(a) loan, the percentage of guaranty is calculated as if the loans are combined, but the Upfront Fee is based solely on the maturity of each loan.

d) If a short-term 7(a) loan that was made within 90 days of a long term 7(a) loan is renewed and the maturity is extended beyond 12 months, the Upfront Fee calculated at the time of renewal would equal the fee that would have been charged if both 7(a) loans were originally long term. The amount owed SBA at the time of renewal would equal the recalculated Upfront Fee less the amount paid at the time of original approval.

e) This rule also applies to any subsequent increases to either of the 7(a) loans made within the 90 day period, even if one of the loans subsequently is paid in full.

iii. When the Upfront Fee Must be Paid (13 CFR § 120.220(b)):

The 7(a) Lender must pay the Upfront Fee to SBA as follows:

a) Short-term loans (maturities of 12 months or less):

i) The 7(a) Lender must pay the Upfront Fee through www.pay.gov within 10 business days from the date the SBA Loan Number is assigned. If the fee is not received within 10 business days after issuance of the SBA Loan Number, SBA will cancel the guaranty.

ii) For EWCP loans re-issued after 12 months, each time the loan is re-issued it is a new loan, and another Upfront Fee is due. SBA earns the short-term Upfront Fee when the SBA loan number is issued.

iii) The 7(a) Lender may only charge the Upfront Fee to the Borrower after the 7(a) Lender has paid the Upfront Fee.

b) Loans with maturities in excess of 12 months:

i) The 7(a) Lender must pay the Upfront Fee to SBA within 90 days of the date of loan approval. If the Upfront Fee is not paid within 90 days, the guaranty will be cancelled. The 7(a) Lender may charge the Upfront Fee to the Borrower after initial disbursement; however, the first disbursement may not be made solely or primarily for the purpose of paying the Upfront Fee.

ii) Notification of Fee Due: When SBA issues an SBA loan number, this is the Lender's notification that an Upfront Fee is due and payable within 90 days. SBA may, but is not required to, inform the 7(a) Lender when the Upfront Fee has not been received by SBA within the required time frame. Neither the issuance by SBA of any notice of non-payment nor the receipt of any notice of non-payment by the 7(a) Lender waives the 7(a) Lender's obligation to pay the fee within 90 days of approval. In addition, the obligation to pay the Upfront Fee to SBA is not contingent upon the Borrower having paid the fee to the 7(a) Lender.

c) THE DUE DATE FOR UPFRONT FEE PAYMENT MAY NOT BE WAIVED OR EXTENDED EVEN IF THE DISBURSEMENT PERIOD IS EXTENDED.

iv. Additional Upfront Fee for Loan Increases.

a) When a 7(a) loan is increased, additional appropriations are committed, and an additional Upfront Fee is due. The additional fee is based on the rules in effect at the time the loan was originally approved. Therefore, the amount of the additional Upfront Fee due for an increase will equal what the Upfront Fee would have been if the increase was part of the original loan amount, less the amount of the Upfront Fee (if already remitted).

b) The additional Upfront Fee associated with the increase must be paid electronically within 30 days from the date the increase was approved, or the total loan guaranty will be cancelled.

c) On loans that have been initially disbursed, the Upfront Fee associated with any increase approved by SBA must be paid to SBA, whether or not the increase is subsequently cancelled.

v. Additional Upfront Fee for Extensions of Short-Term Loans.

a) When the maturity of a short-term 7(a) loan is extended beyond 12 months, an additional Upfront Fee is due. The 7(a) Lender may email FSC.Servicing@sba.gov for assistance. The additional fee must be paid electronically within 30 days from the date the 7(a) Lender agrees to the extension, or the total loan guaranty will be cancelled. The 7(a) Lender may charge the additional fee to the Borrower after the 7(a) Lender has

notified SBA that the maturity has been extended and has paid the additional Upfront Fee.

b) No additional Upfront Fees will be owed for loans extended beyond their original maturity date when SBA determines the extension is to effect collection and no new funds are disbursed, regardless of the original maturity.

vi. Method of Upfront Fee Payment.

The 7(a) Lender must electronically pay the Upfront Fee either by using their existing SBA-approved bulk ACH method or through www.pay.gov. When using www.pay.gov, select "form type 1544" and select "guaranty." The loan must have been approved and an SBA Loan Number issued in order to use www.pay.gov. Any questions regarding this requirement can be emailed to paymentservices@sba.gov.

vii. Reinstatement of Guaranty After Cancellation.

If SBA cancelled its guaranty because the 7(a) Lender did not pay the Upfront Fee, the 7(a) Lender may request that SBA consider reinstating its guaranty. The 7(a) Lender must submit a written request, via email, to either the 7(a) Loan Guaranty Processing Center (LGPC) at 7aLoanMod@sba.gov if not fully disbursed, or to the Commercial Loan Servicing Center (CLCS) at FSC.Servicing@sba.gov if the loan is fully disbursed, in accordance with Section B, Ch 6, "SBA Terms and Conditions through Disbursement for all 7(a) Loans". If SBA reinstates the guaranty, the required Upfront Fee must be electronically paid within 30 days from the date of reinstatement, or the guaranty will be cancelled. The request must include the following:

a) SBA Loan Number and the SBA Loan Name;

b) A certification that there has been no unremedied adverse change in the financial condition, organization, operations, or fixed assets of the Borrower or Operating Company since the date of application for guaranty;

c) If the loan has been disbursed in whole or in part, a certification that the loan is current, the 7(a) Lender has been reporting the loan on all SBA Form 1502 monthly reports since the loan was disbursed, and the 7(a) Lender has been paying the Lender's Annual Service Fee in a timely manner on this loan; and

d) A complete written explanation as to why the 7(a) Lender failed to pay the Upfront Fee and what the 7(a) Lender has done to correct any deficiencies in its procedures.

viii. Upfront Fee Refunds (13 CFR §120.220(c)).

The Upfront Fee is based on the amount that SBA has approved prior to the loan being closed and initially disbursed. Any request by the 7(a) Lender to decrease the approved amount must be approved by SBA prior to the date the loan is closed and initially disbursed by the 7(a) Lender in order for the Upfront Fee to be reduced. The 7(a) Lender must submit a request to the Commercial Loan Servicing Center (CLSC) via the SBA Loan System for an adjustment to the approved amount of the loan and Upfront Fee. Email questions on guaranty fees to FSC.Servicing@sba.gov.

a) Full refund: The Upfront Fee may be refunded only for a loan with a maturity of more than 12 months and when the loan has not been closed and initially disbursed and the 7(a) Lender submits a request to SBA via the SBA Loan System to cancel the guaranty. Once a loan has been initially disbursed, no refund is permitted. For loans with a maturity of 12 months or less, once the SBA loan number has been issued, no refund will be given.

b) Partial refund: If SBA approves the cancellation of a portion of the loan prior to the loan being closed and initially disbursed, SBA will adjust the Upfront Fee payable to reflect the new loan amount and refund the excess amount if the fee has already been paid. If the loan has been closed and initially disbursed, no refund is permitted.

b. 7(a) Lender's Annual Service Fee (Lender's Annual Service Fee) (13 CFR § 120.220(f)).

The 7(a) Lender must pay SBA a Lender's Annual Service Fee. The fee is based on the outstanding principal balance of the guaranteed portion of the loan at the time of SBA Loan approval. SBA specifies the amount of the fee each fiscal year for all loans approved during that year through an Information Notice. This fee cannot be charged to the Borrower.

When multiple 7(a) loans are made within 90 days of each other, the Lender's Annual Service Fee is set for each loan on a standalone basis without respect to any other loans made (i.e., the loans are not aggregated).

The 7(a) Lender pays this fee on a monthly basis with submission of SBA Form 1502, "Guaranty Loan Status and Remittance Form." SBA may charge the 7(a) Lender a late fee if the on-going guaranty fee is not paid timely.

For EWCP payment options, see Section B, Ch. 5, Para. B.4.e., Payment Options for EWCP Ongoing Guaranty Fee.

Note: The fee will be listed in the SBA Terms and Conditions, and it is the 7(a) Lender's responsibility to ensure that the SBA Terms and Conditions includes the correct fee.

2. Fees and Expenses the Lender May Collect from the Applicant or Borrower

   In 13 CFR § 120.221, SBA provides specific guidance on the fees a 7(a) Lender or its Associates may collect from an Applicant or Borrower in connection with an SBA-guaranteed loan.

   a. Packaging Fees 13 CFR § 120.221(a)

      i. The Lender may charge an applicant reasonable fees (customary for similar Lenders in the geographic area where the loan is being made) for packaging. "Packaging services" include assisting the Applicant with completing one or more applications, preparing a business plan, cash flow projections, and other documents related to the application. The Applicant may not be charged for the same service by two different entities, and, if the Lender engages the services of a Lender Service Provider (LSP), it may not pass through to the Applicant any fees charged for work performed by the LSP.

      ii. The Lender must advise the Applicant in writing that the Applicant is not required to obtain or pay for unwanted services. The Lender must itemize for the Applicant in writing any fees charged in association with the 7(a) loan. Itemization means listing the category of fees identified under 13 CFR § 120.221. SBA may review these fees at any time. Lender must refund any such fee considered unreasonable by SBA.

      iii. As part of its packaging fee, Lenders may charge fees associated with technology services (whether developed internally or purchased from a third party) for software or technology used in connection with preparing SBA loan documents, underwriting, or closing the SBA-guaranteed loan. Note: Entities providing technology services that include underwriting are considered to be LSPs and must be providing their services to the Lender under an SBA-reviewed LSP Agreement.

      iv. SBA permits the Lender to charge the Applicant a flat fee of up to $2,500 per loan without documenting the service performed. The Lender must disclose any amounts charged to the Applicant by the Lender in the SBA Loan System.

      v. For fee amounts in excess of $2,500, the Lender must complete an SBA Form 159 in accordance with Paragraph D.8., Disclosure of Fees – SBA Form 159, in this Chapter.

         a) For fees charged on an hourly rate, the fees must be reasonable and customary for the services actually performed and consistent with fees charged on an hourly rate for the Lender's similarly-sized non-SBA guaranteed commercial loans.

         b) For fees charged based on a percentage of the loan amount, the fee may not exceed what the Lender charges on a percentage basis for the

Lender's similarly-sized non-SBA guaranteed commercial loans or the following, whichever is less:

i) 5% for loans $150,000 or less;

ii) 3% for loans in excess of $150,000;

iii) the maximum fee that may be charged to an Applicant on a percentage basis is $30,000.

vi. The Lender may not split a loan into two loans for the purpose of charging an additional fee to the Applicant. Even if there is a legitimate business need for the Applicant's loan request to be split into two loans (e.g., a term loan and a line of credit), the Lender may only charge the Applicant one fee within the maximums set forth above, based on the combined loan amounts. However, it is not SBA's intention to restrict a Lender from charging a new fee if an Applicant subsequently returns to the Lender to apply for a new loan for a different project or purpose. (Loans approved more than 90 days apart are considered to be for a different project or purpose.)

b. Extraordinary Servicing Fee. 13 CFR § 120.221(b)

i. A Lender may not charge the Borrower a servicing fee on an SBA-guaranteed loan unless the servicing fee is to cover expenses for extraordinary servicing requirements connected with the loan. Such a fee may not exceed 2% per year on the outstanding balance of the part of the loan requiring special servicing, unless otherwise specified in Section B, 7(a) Loan Program Specific Requirements. Examples of extraordinary servicing fees include amounts to service construction loans or monitor accounts receivable and inventory collateral in asset-based lending. In addition, if the Lender charges an extraordinary servicing fee on its similarly-sized, non-SBA guaranteed commercial loans, it may not charge a higher fee on its SBA-guaranteed loans. If the Lender does not charge an extraordinary servicing fee on its similarly-sized, non-SBA guaranteed commercial loans, it may not charge an extraordinary servicing fee on its SBA-guaranteed loans.

ii. Lenders must obtain SBA's prior written approval for the fees in Subparagraph b. i. and b. ii. above and must include the extraordinary servicing fees to be charged to administer the loan/line in its credit memorandum. Lenders submitting applications under delegated authority must enter the amount of the fee to be charged in the SBA Loan System and certify in the credit memorandum that the fee is reasonable and prudent based on the level of extraordinary effort required. SBA's issuance of a loan number will constitute its prior written approval of the fees, subject to SBA's subsequent review of the fees for reasonableness. SBA will review such fees when conducting Lender oversight activities and at time of guaranty purchase.

If SBA determines the fee is excessive, the Lender must reduce the fee to an amount SBA deems reasonable, refund any sum in excess of that amount to the Borrower, and refrain from charging or collecting from the Borrower any funds in excess of the amount SBA deems reasonable. SBA's guaranty does not extend to extraordinary servicing fees and, at time of guaranty purchase, SBA will not pay any portion of such fees.

iii. The following actions do not qualify as extraordinary servicing and therefore a participating Lender is prohibited from collecting fees for these services:

a) Changing the installment amount to avoid circumstances where the required payment amount will not be sufficient to pay the loan in full by the maturity date;

b) Changing the installment amount after a deferment;

c) Providing the release or exchange of collateral (standard out-of-pocket expenses such as recordation fees are permitted); or

d) Any modification to the repayment terms of the note.

c. Out-of-Pocket Expenses. 13 CFR § 120.221(c)

i. The Lender may collect from the Applicant necessary out-of-pocket expenses such as filing or recording fees, photocopying, delivery charges, collateral appraisals and environmental investigation reports that are obtained in compliance with SBA policy, and other direct charges related to loan closing. These costs must be itemized and kept in the loan file for SBA's review.

ii. Fees charged for legal services must be for services performed by a licensed attorney, or someone working under the licensed attorney's direct supervision, regardless of whether the attorney is in-house or outside counsel.

a) Lenders may be reimbursed by the Applicant for the direct costs (including reasonable overhead) of legal services performed by the Lender's in-house counsel in connection with an SBA-guaranteed loan, but in no event may the Lender be reimbursed for an amount that would exceed the cost of outside counsel.

b) In accordance with 13 CFR § 120.221(e), charges for legal services must be charged on an hourly basis. The Lender or its Associate may not pass on to the Applicant/Borrower any cost of legal services not calculated on an hourly basis for services provided in connection with the Applicant/Borrower's transaction.

iii. Direct costs associated with out-of-pocket expenses described in this section in connection with the loan closing should not be reported on SBA Form 159,

but must be available for SBA review when conducting lender oversight activities.

d. Late Payment Fee. 13 CFR § 120.221(d)

Lenders may charge the Borrower a late payment fee not to exceed 5% of the regular loan payment when the Borrower is more than 10 days delinquent on its regularly scheduled payment. The fee is the property of the Lender and is not shared with the investor if the loan is sold into the Secondary Market. SBA's guaranty does not extend to late fees and, at time of guaranty purchase, SBA will not pay any portion of such fees.

e. Assumption Fee.

Lenders should review SBA's SOP 50 57, 7(a) Loan Servicing and Liquidation, for procedures to process an assumption request.

i. In the case of an assumption of the loan by another entity, SBA does not require a new guaranty fee, and lien positions are often maintained eliminating the need for recording fees. As an incentive for a 7(a) Lender to retain an existing loan, SBA allows a 7(a) Lender to charge an assumption fee that is consistent with its assumption fee the 7(a) Lender charges on its non-SBA guaranteed loans. The fee must be reasonable in relation to services provided and cannot exceed 1 percent of the principal balance outstanding at time of assumption. SBA's guaranty does not extend to assumption fees and, at time of guaranty purchase, SBA will not pay any portion of such fees.

ii. This fee may be paid by the seller or the assumptor.

3. Fees the Borrower Pays to SBA

Subsidy Recoupment Fee 13 CFR § 120.223

For loans with a maturity of 15 years or longer, the Borrower must pay to SBA a Subsidy Recoupment Fee when the Borrower voluntarily prepays more than 25% of its loan in any 1 year during the first 3 years after first disbursement. The fee is 5% of the prepayment amount during the first year, 3% the second year, and 1% in the third year. The Subsidy Recoupment Fee would also apply to any loan originally made with a maturity of less than 15 years, when the maturity is extended to 15 years or more during the first 36 months of the loan. Any prepayments made prior to the maturity extension are subject to the subsidy recoupment fee. SBA does not consider death that results in a prepayment a voluntary occurrence. No determination by SBA is required in this circumstance, and the 7(a) Lender must confirm and document their file. If the 7(a) Lender otherwise believes that the prepayment of the loan is not voluntary, the 7(a) Lender may submit a request for a determination, with the 7(a) Lender's supporting analysis, by email to the Commercial Loan Servicing Center (CLSC) at FSC.Servicing@sba.gov. The CLSC will submit the request, along with its

recommendation to the Director of the Office of Financial Program Operations (D/OFPO) and the D/FA or designee for a joint determination as to whether a prepayment is involuntary.

4. Prohibited Fees

   Any fee not expressly permitted in 13 CFR § 120.221 is prohibited. For example, 7(a) Lenders and/or their Associates may not:

   a. Require the Applicant or Borrower to pay the 7(a) Lender, a 7(a) Lender's Associate, or any party designated by either, any fees or charges for goods or services, including insurance, as a condition for obtaining an SBA-guaranteed loan;

   b. Charge the Borrower any commitment, bonus, origination, broker, commission, referral, or similar fees;

   c. Charge points or add-on interest;

   d. Charge prepayment fees;

   e. Charge renewal fees; or

   f. Share any portion of the premium received from the sale of an SBA-guaranteed loan in the Secondary Market with a Service Provider, Packager, or other non-employee loan referral source.

## D. 7(A) LOAN PROGRAM AND USE OF AGENTS

SBA permits a third party to charge an Applicant fees for packaging and other services. Prior to any services being provided, the 7(a) Lender must advise the Applicant in writing that the Applicant is not required to obtain or pay for unwanted services.

1. Use of Agents in the 7(a) Loan Program

   a. SBA regulations at 13 CFR Part 103 govern the activities of Agents, the disclosure of fees, and the circumstances that would result in revocation or suspension of the Agent's privilege to conduct business with SBA.

      i. SBA expects 7(a) Lenders to exercise due diligence and prudent oversight of their third party vendors, including LSPs, and other loan agents.

      ii. Prudent oversight should include having written policies governing such relationships and monitoring performance of loans referred by an Agent or where an Agent provided assistance.

      iii. SBA will review evidence of such due diligence and oversight of such relationships when conducting lender oversight activities.

      iv. Federally-regulated 7(a) Lenders are reminded that they must comply with the requirements of their primary Federal Financial Institution Regulator

regarding third party vendors.

b. The Director of SBA's Office of Credit Risk Management may, for good cause, suspend or revoke the privilege of an Agent to conduct business with the government. The suspension or revocation will remain in effect during any administrative proceedings under SBA regulations at 13 CFR Part 134. The meaning of "good cause" can be found at 13 CFR § 103.4.

c. Agents and Privacy Act Considerations.

Proprietary information is protected by the Right to Financial Privacy Act and the Privacy Act. Private information about a loan cannot be discussed with anyone who claims to be an Agent for an Applicant or 7(a) Lender without evidence of representation. SBA may require that an Agent supply written evidence of their authority to act on behalf of an Applicant or 7(a) Lender as a condition of revealing any information about the Applicant's or 7(a) Lender's current or prior dealings with the SBA.

d. Employment of Agent by Applicant.

7(a) Lenders and Agents must clearly inform any Applicant that the SBA does not require the use of an Agent for packaging or referring a loan application. When an Applicant employs an Agent:

i. The Agent may bill and be paid by the Applicant for providing packaging services as long as compensation is reasonable and customary for those services; the compensation complies with SBA Loan Program Requirements; and the compensation is not contingent on the loan being approved or closed.

ii. The Agent who works for an Applicant as a packager may also work as a Loan Referral Agent for the Applicant and receive a referral fee from the Applicant. However, if the Agent performs multiple services for the Applicant, the total fee for all services may not exceed the stated maximums in Paragraph D.7. below.

iii. The Agent may be a Loan Referral Agent for a 7(a) Lender and a Packager for an Applicant, provided both the Applicant and the 7(a) Lender are aware of both relationships, and the Agent does not receive a referral fee from the Applicant or a packaging fee from the 7(a) Lender.

e. Employment of Agent by 7(a) Lender (not an LSP).

i. When a 7(a) Lender has decided to approve a loan application and needs assistance with the preparation of the paperwork for the application to SBA, the loan closing, or preparation of the loan to sell it on the Secondary Market, the 7(a) Lender may use an Agent.

ii. The compensation for these services should be reasonable and customary for the services actually provided, and compensation for services associated with preparation of the application through loan closing cannot be contingent upon the loan being approved or closed by SBA.

iii. The Agent must bill and be paid by the 7(a) Lender for all services and the 7(a) Lender may not pass these charges through to the Applicant or pay them with SBA-guaranteed loan proceeds under any circumstances, including with loan proceeds allocated to working capital.

2. Agents

13 CFR § 103.1(a)

a. SBA defines an "Agent" to mean an authorized representative, including an attorney, accountant, consultant, packager, lender service provider, or any other individual or entity representing an Applicant or participant by conducting business with SBA. Lenders may not use Lender Service Providers or any type of Agent that is not located in the United States, its territories, or possessions.

b. For Lender Service Providers, SBA reviews the written agreement between the Lender and the Lender Service Provider, thus SBA Form 159 is not required for the services provided by the Lender Service Provider to the Lender. (13 CFR § 103.5(c)) Fees paid by the Lender to the Lender Service Provider cannot be passed onto the Applicant.

c. For Agents not covered by an SBA-reviewed LSP Agreement, whether paid by the Applicant or the Lender, SBA Form 159 must be completed and signed by the Applicant, the Agent, and the Lender. When an Agent is paid by the Lender, the Lender must identify the Agent on SBA Form 159 and the Lender and Applicant must sign the form. If the Lender is acting as both Lender and Agent, the Lender must sign twice.

d. The only situation where an Agent can receive compensation from both the Lender and the Applicant is when the Agent is providing different services by providing packaging services to the Applicant and receiving a referral fee from the Lender. (13 CFR § 103.4(g))

e. The SBA does not allow contingency fees (fees paid only if the loan is approved or closed) or charges for services which are not reasonably necessary in connection with an application.

f. The SBA loan may not refinance a debt where the creditor is an Agent involved in the Loan (e.g. a Referral Agent).

3. Referral Agents

13 CFR § 103.1(f)

"Referral Agent" means a person or entity that identifies and refers an Applicant to a Lender or a Lender to an Applicant. The referral agent may be employed and compensated by either an Applicant or a Lender, but not both. Each referral agent, including loan packagers, must disclose the name of its customer and all fees charged in connection with the SBA loan transaction on SBA Form 159.

4. Packager

   13 CFR § 103.1(e)

   a. "Packager" means an Agent who is employed and compensated by an Applicant or Lender to prepare the Applicant's application for financial assistance from SBA. The packager may be the Lender.

   b. For 7(a) loans, if a CDC employee performs packaging or loan referral services within the scope of their CDC employment, both the CDC and the employee are Agents. If a CDC employee acts as a Packager or Referral Agent outside the scope of their employment, the CDC is not considered an Agent.

5. Lender Service Provider

   13 CFR § 103.1(d)

   a. "Lender Service Provider" means an Agent who carries out Lender functions in originating, disbursing, servicing, or liquidating a specific SBA business loan or loan portfolio for compensation from the Lender.

   b. A Lender must have a continuing ability to evaluate, process, close, service, liquidate and litigate small business loans (13 CFR § 120.410). A Lender may contract with a third party (Lender Service Provider (LSP)) to assist the Lender with one or more of these functions. However, the Lender itself, not the LSP, must be able to demonstrate that it exercises day-to-day responsibility for evaluating, processing, closing, disbursing, servicing, liquidating, and litigating its SBA portfolio. SBA determines whether or not an Agent is an LSP on a loan-by-loan basis. If an Agent meets the definition of an LSP, a formal agreement between the Agent and Lender is required and must be reviewed by SBA.

   c. All participating Lenders must submit each LSP agreement to the LGPC for review. Lenders may submit the agreements to LSPagreements@sba.gov. If there are any changes to an LSP agreement after review by SBA, the Lender must submit the revised agreement to SBA for review.

   d. SBA will investigate any complaint by an Applicant, Lender, or any other participant in an SBA program, concerning the activity, services completed, or fees charged by any LSP.

   e. SBA reserves the right to audit compliance with any SBA-reviewed LSP agreement.

6. Lender Service Provider Agreements

   13 CFR § 103.1(d)

   A 7(a) Lender may contract with a third party LSP to assist the 7(a) Lender with one or more lender functions. The LSP must perform these services under a written LSP Agreement between the 7(a) Lender and the LSP that must be submitted to SBA for review.

   a. A 7(a) Lender must have a continuing ability to evaluate, process, close, service, liquidate and litigate small business loans (13 CFR § 120.410).

   b. The 7(a) Lender itself, not the LSP, bears full responsibility for all aspects of its SBA Loan operation and must be able to demonstrate that it exercises day-to-day responsibility for evaluating, processing, closing, disbursing, servicing, liquidating, and litigating its SBA portfolio.

   c. An LSP may only receive compensation from the 7(a) Lender for services provided under an SBA-reviewed LSP Agreement. Such charges must not be passed on to the Applicant or paid out of the SBA-guaranteed loan proceeds.

   d. Services performed by the LSP for the 7(a) Lender in accordance with the LSP Agreement are not reported on SBA Form 159. (13 CFR § 103.5(c)).

   e. The following are examples of when SBA considers an Agent to meet the definition of an LSP:

      i. An individual or entity engaged by a 7(a) Lender to provide services for the purposes of obtaining Federal financial assistance that include interaction with the Applicant either in-person or through the use of technology, to request or obtain financial information that will be provided to the 7(a) Lender or SBA. This includes Agents who:

         a) Perform any pre-qualification review based on SBA's Loan Program Requirements or the 7(a) Lender's internal policies prior to submitting the Applicant's information to the 7(a) Lender; or

         b) Provide to the 7(a) Lender an underwritten application, whether through the use of technology or otherwise.

      ii. Entities providing technology services to a 7(a) Lender that include underwriting.

   f. SBA will investigate any complaint by an Applicant, 7(a) Lender or any other participant in an SBA program concerning the activity, services completed, or fees charged by any LSP.

   g. An LSP Agreement may not grant the LSP power of attorney to act on behalf of the 7(a) Lender.

h. If the 7(a) Lender engages an LSP to handle its SBA Borrower payments:

   i. The funds must be held in an account in the 7(a) Lender's name, not the name of the LSP; however, consistent with the LSP Agreement, the LSP may be permitted limited access to the account in order to process Borrower payments;

   ii. For those loans where the guaranteed portion has been sold on the Secondary Market, the account also must be properly titled in accordance with SBA Form 1086, "Secondary Participation Guaranty Agreement."

   iii. The LSP may not commingle any funds from multiple lenders; there must be separate accounts for each of its lender clients.

   iv. The LSP may not net its fee out of any Borrower payments or other funds collected on the 7(a) Lender's behalf.

i. All participating 7(a) Lenders must submit each LSP agreement to the LGPC for review at LSPagreements@sba.gov. If there are any changes to an LSP agreement after review by SBA, the 7(a) Lender must submit the revised agreement to SBA for review. SBA reserves the right to audit compliance with any SBA-reviewed LSP agreement.

j. Upon the termination or cancellation of any LSP Agreement, a copy of the notification of termination must be sent to LSPagreements@sba.gov. The notification must include the date of termination and the 7(a) Lender's SBA Location ID.

k. SBA does not provide a form of LSP Agreement but expects 7(a) Lenders and LSPs to negotiate the terms of the contract to meet the needs of the 7(a) Lender. Each agreement must include the following:

   i. Identification of both parties including full legal name, trade name or dba, address, and contact person's name, address, phone number, email address, and the 7(a) Lender's Location ID Number.

   ii. Services: The contract must specifically identify the services that will be performed by the LSP.

   iii. 7(a) Lender's responsibility: There must be a statement that the 7(a) Lender bears full responsibility for all aspects of its 7(a) loan operation, including, but not limited to, approvals, closings, disbursements, servicing actions and due diligence. The LSP only provides assistance to the 7(a) Lender. If an LSP is authorized to access SBA's Capital Access Financial System (CAFS), including the SBA Loan System, on behalf of a 7(a) Lender, the 7(a) Lender acknowledges it is responsible for all entries and certifications made into CAFS by the LSP.

iv. If the 7(a) Lender plans to engage an LSP to handle its SBA Borrower payments, the LSP Agreement must describe the specific parameters governing the LSP's access to the funds;

v. Compensation: The compensation must be specifically explained as to what will be charged for each type of service and must state that the fees are for services actually performed.

a) Fees related to assisting the 7(a) Lender with packaging, processing, or underwriting cannot be contingent on whether the loan is approved or closed.

b) The contract must state that all compensation paid to the LSP will be paid by the 7(a) Lender and that the 7(a) Lender and the LSP are prohibited from charging the Applicant for the same services.

c) **The 7(a) Lender and the LSP cannot share in any Secondary Market premium**.

d) The billing for loan packaging or for other loan processing services must identify the Applicant's name.

vi. Term: The full term of the contract including renewal options must be stated in order for SBA to determine if it is reasonable. In addition, the contract must clearly identify terms and conditions satisfactory to SBA that permit either party to terminate the contract prior to its expiration date on a reasonable basis (usually 60 days or sooner for cause).

vii. The contract also must include the following statements or disclosures:

a) The LSP will not assume a portion of the risk of the un-guaranteed portion of any loan.

b) Disclosure by the LSP of any affiliations with other financial institutions, commercial lenders, CDCs, CUSOs, other LSPs, or loan brokers.

c) Disclosures of any prior or existing relationship other than the contractual one created by the agreement, or a statement that no such relationship exists.

d) The agreement is subject to all applicable laws, regulations, and policies including all SBA Loan Program Requirements.

e) In the event this Lender Service Provider Agreement conflicts with any other contract or agreement between the parties, now or in the future, this Lender Service Provider Agreement will control with respect to the 7(a) Lender's SBA Loan portfolio.

viii. 7(a) Lenders are responsible for the actions of their LSPs and must ensure that they comply with all applicable laws and regulations governing

confidentiality. 7(a) Lenders should consult with their Counsel on appropriate language to be included in their LSP Agreements.

ix. The contract must not evidence any actual or apparent conflict of interest or self-dealing on the part of any of the 7(a) Lender's officers, management, or staff.

7. Fees an Agent May Charge an Applicant for Packaging and Other Services

a. An Agent may charge an Applicant for:

i. Packaging services to assist the Applicant with completing one or more applications, preparing a business plan, cash flow projections, and other documents related to the application; and

ii. Other services that include consulting as to the amount and type of financing needed and broker or referral fees. (As stated above, the 7(a) Lender and its Associates are prohibited from charging an Applicant for these services.)

b. Regardless of who pays the Agent, the fees must be reasonable and customary for the services actually performed and, for those Lenders with non-SBA guaranteed portfolios, must be consistent with those fees charged on the 7(a) Lender's similarly-sized, non-SBA guaranteed commercial loans. If the 7(a) Lender does not charge a particular fee on its similarly-sized, non-SBA guaranteed commercial loans, it may not charge the fee on its SBA guaranteed loans.

c. An Agent may charge an Applicant fees for packaging and other services based on an hourly rate or on a percentage of the loan amount. In either case, all fees over $2,500 must be supported by documenting the service performed.

i. For fees charged to an Applicant on an hourly rate, there is no maximum, but the fees must be reasonable and customary for the services actually performed. The hourly rate and time spent on each service must be documented.

ii. For fees charged to an Applicant based on a percentage of the loan amount, the fee may not exceed (if multiple services are provided to the Applicant, the combined fee for all services cannot exceed the stated maximums below):

a) 3 percent on loans of $50,000 or less;

b) 2 percent for loans between $50,000 and the first $1,000,000 and 0.25 percent on the portion over $1,000,000; however,

c) The maximum fee that may be charged in the aggregate to an Applicant on a percentage basis is $30,000.

iii. SBA does not allow an Agent to charge an Applicant:

a) A standard or flat fee charged to all Applicants;

b) Contingency fees (fees paid only if the loan is approved or closed); or

c) For services that are not reasonably necessary in connection with an application.

**d.** SBA may review these fees at any time. Agents must refund any fee considered unreasonable or impermissible by SBA.

e. Review of Agent Fees.

i. 7(a) Lenders must review all services and related fees charged to either the 7(a) Lender or the Applicant by any Agent to determine if the fees are necessary and reasonable when:

a) There is an indication from a third party that an Agent's fees might be excessive; or

b) An Applicant complains about the fees charged by an Agent.

ii. In cases where fees appear to be unreasonable or impermissible, 7(a) Lenders should contact the D/OCRM to report the fees.

**iii.** If an SBA investigation determines an Agent fee is excessive, the Agent must reduce the fee to an amount SBA deems reasonable, refund any sum in excess of that amount to the Applicant, and refrain from charging or collecting from the Applicant any funds in excess of the amount SBA deems reasonable.

8. Disclosure of Fees – SBA Form 159

Section 13 of the Small Business Act (15 U.S.C. § 642) requires that an Applicant identify the names of Persons (as defined in 13 CFR § 120.10) engaged by or acting on behalf of the Applicant for the purpose of expediting the application and the fees paid or to be paid to any such Person. SBA regulations at 13 CFR § 103.5 require the Applicant, 7(a) Lender, and any Agent to execute and provide to SBA a compensation agreement ("Agreement"). Each Agreement governs the compensation charged for services rendered or to be rendered to the Applicant or 7(a) Lender in any matter involving SBA assistance.

a. 7(a) Lenders must identify in the SBA Loan System whether the 7(a) Lender charged any fees and the amount of those fees, and whether an Agent was involved in any way with the transaction.

b. When an Agent was involved in the transaction, the 7(a) Lender must provide the name, street address, city, state, and zip code of the Agent. Failure to do so may result in a finding by OCRM when conducting lender oversight activities. SBA Form 159 can be generated using the SBA Loan System.

c. For Agents other than LSPs performing duties under an SBA-reviewed LSP Agreement, if the Agent is paid by an Applicant or a 7(a) Lender, an SBA Form 159 must be completed in accordance with form instructions and signed by the Applicant, the Agent, and the 7(a) Lender. Separate SBA Forms 159 are required

for each Agent who provides services to the Applicant. Failure of an Agent to fully complete and execute the required SBA Form 159 may result in suspension or revocation of the Agent's privilege to conduct business with SBA under 13 CFR Part 103.

d. SBA Form 159 "Fee Disclosure Form and Compensation Agreement"

i. Information on this form will be used to monitor fees charged by Agents and the relationship between Agents and 7(a) Lenders. 7(a) Lenders must complete all appropriate data fields on SBA Form 159 in accordance with the form instructions. For example, the seven-digit FIRS number must be included exactly as assigned by SBA and without any extra characters.

ii. If the aggregate compensation for all fees provided by the same Agent exceeds $2,500, an itemization of the compensation received and supporting documentation must be attached to the Form 159.

a) When an Agent charges an Applicant in connection with multiple applications (for example, an Applicant is seeking a term loan and a revolver):

i) Separate SBA Forms 159 must be completed for each application.

ii) Fees are aggregated to establish the $2,500 threshold for itemization.

b) When the Agent provides multiple services to an Applicant in connection with the same loan application (for example, an Agent is providing both loan packaging and referral services to the Applicant), each service must be separately reported on the same SBA Form 159. For example:

i) In the "Type of Agent" section, select both the "Independent Loan Packager" and the "Referral Agent/Broker" boxes; and

ii) In the "Type of Service" table, separately itemize the amounts paid in each appropriate box.

c) In-kind compensation (i.e., non-monetary contributions for goods or services) paid or to be paid by the 7(a) Lender must be itemized.

iii. The following are not considered Agents for purposes of this Agreement and are not required to complete SBA Form 159:

a) Applicant's accountant for the preparation of financial statements required by the Applicant in the normal course of business and not related to the loan application;

b) A state-certified or state-licensed appraiser employed by the 7(a) Lender to appraise collateral in connection with the SBA Loan;

c) An LSP performing services for the 7(a) Lender under an SBA-reviewed LSP agreement;

d) An individual who is a Qualified Source and employed by the 7(a) Lender to conduct an independent business valuation in connection with the SBA Loan;

e) An environmental professional employed by the 7(a) Lender to conduct an environmental assessment of the collateral in connection with the SBA Loan;

f) Any attorney in connection with the SBA Loan closing; and

g) A real estate agent who is receiving a commission for the sale of real estate in connection with the SBA Loan.

e. When required, 7(a) Lenders must submit a copy of the completed SBA Form 159, signed by all applicable parties, along with any required supporting documentation electronically to SBA's Capital Access Financial System (CAFS) at https://caweb.sba.gov. A separate Form 159 must be completed for each application when an Agent provides services to an Applicant in connection with multiple applications. The completed form and any required supporting documents must be uploaded into E-Tran Servicing, or successor SBA Loan System after the initial disbursement on the loan in conjunction with the Lender's monthly 1502 report. Submission must be within two SBA Form 1502 reporting cycles from the date of initial disbursement. 7(a) Lenders are required to retain an original signature version of the form and all supporting documentation in their files for compliance review purposes.

## E. 504 LOAN PROGRAM FEES AND USE OF AGENTS

1. Borrower's Deposit

a. At the time of application, the CDC may require a deposit from the Borrower of $2,500 or 1% of the Net Debenture Proceeds, whichever is less. For additional information relating to this fee, see 13 CFR § 120.935.

b. Agreements Regarding the Deposit:

A written agreement between the CDC and the Applicant should include the following:

i. If the CDC or SBA declines the application, the deposit will be refunded in full within 10 business days after decline, including any period for reconsideration;

ii. If SBA approves the loan, the deposit may be applied toward the CDC processing fee described in 13 CFR § 120.883; and

iii. If the Applicant withdraws its loan application at any time before SBA issues the SBA Terms and Conditions, the CDC may deduct its reasonable and necessary costs incurred in packaging and processing the loan application. Such costs must be documented and cannot be a percentage of the loan. Any remaining deposit balance must be remitted to the Applicant within 10 business days of the withdrawal.

c. A copy of the agreement must be placed in the CDC's file.

2. Allowable Fees

The fees that a 504 Borrower may be charged can be found at: 13 CFR §§ 120.971, 120.972, 120.883(e) and 120.882(g)(4) and are described in the table below.

| Fees that a 504 Borrower May be Charged | | |
|---|---|---|
| **CDC Fees** | | |
| (1) Processing fee (Packaging fee) | Up to 1.5% of the Net Debenture | Paid by Borrower to CDC. |
| (2) Closing Fee | Maximum of $10,000 may be financed from the debenture proceeds. | CDC may charge a reasonable closing fee –sufficient to reimburse it for the expenses of its in-house or outside legal counsel, and other miscellaneous closing costs. Paid by Borrower. |
| (3) Servicing fee (monthly) | Minimum of 0.625%/year. Maximum of 2%/year Note: Maximum 1.5% for rural areas and 1% for everywhere else without prior SBA approval. | Based on the unpaid principal balance of the loan – paid by Borrower to CDC |
| (4) Late fees | Loan payments received after the 15th of each month may be subject to a late payment fee of 5% of the late payment or $100, whichever is greater. | Collected by CSA (Central Servicing Agent) on behalf of the CDC. |
| (5) Assumption fee | Not to exceed 1% of the outstanding principal balance of the loan being assumed. | Upon SBA's written approval<br>–paid by Borrower to CDC. |
| **CSA Fees** | | |
| Initiation fee | In accordance with the contract between the CSA and SBA. | |
| On-going fee | In accordance with the contract between the CSA and SBA. | |

| Fees that a 504 Borrower May be Charged | | |
|---|---|---|
| **Underwriter's Fees** | | |
| Underwriter's fee for 20 and 25-year Debenture | Upfront fee of 0.4% | Paid by Borrower to Underwriter. |
| Underwriter's fee for 10-year Debenture | Upfront fee of 0.375% | Paid by Borrower to Underwriter. |
| **SBA Fees** | | |
| (1) SBA Guaranty Fee – (up-front fee) | Refer to www.sba.gov for notices on fee updates by fiscal year | One-time fee |
| (2) Annual Fee – (Ongoing fee) | Refer to www.sba.gov for notices on fee updates by fiscal year | Fee is adjusted annually by cohort year (based on date the individual loan was approved) and is charged on the unpaid principal balance of the loan. |
| (3) Participation Fee – Senior Lienholder | 0.50 % of the senior mortgage loan – One -time fee | A one-time fee from the Third Party Lender if in a senior lien position to SBA in the project. The fee may be paid by the Third Party Lender, CDC, or Borrower. |
| (4) CDC Fee | On-going fee to SBA of 0.125% of the outstanding principal balance of the Debenture – Annual Fee | The fee must be paid from the servicing fees collected by the CDC and cannot be paid from any additional fees imposed on the Borrowers (loans approved by SBA after 9/30/1996). |
| (5) Debt Refinancing Without Expansion Supplemental Fee | Refer to www.sba.gov for notices on fee updates by fiscal year | Paid by Borrower. |
| **Funding Fee** | 0.25% of the net Debenture Proceeds | Charged to cover the costs incurred by the trustee, fiscal agent, and transfer agent. |

3. Fees for Other Services

   a. The CDC may be compensated for other services such as packaging and servicing a 7(a) loan or providing assistance unrelated to the 504 loan program to a small business. Such fees are to be charged pursuant to a written agreement, between the CDC and the entity for which the CDC is providing services, setting forth the roles

and relationships of the parties as well as terms and conditions and must be in compliance with SBA Loan Program Requirements. The CDC may not make such assistance a condition of the CDC accepting from a small business an application for a 504 loan.

b. CDC referral fees for locating third party financing (13 CFR § 120.926):

The CDC may earn a fee for this service provided it is:

i. Based upon a contractual agreement between the Third Party Lender paying the referral fee and the CDC; and

ii. Not paid by the Borrower or funded from the debenture proceeds.

c. Fees associated with technology services (whether developed internally or purchased from a third party) may not be passed on to the Borrower. Examples of technology services fees that may not be passed on to the Borrower include:

i. The costs or fees for software or technology used in connection with preparing SBA loan documents, CDC underwriting, or closing the SBA-guaranteed loan;

ii. Acquisition costs or fees for licensing software or software platforms to CDCs solely for the purpose of performing administrative functions (not including any underwriting functions), such as generating SBA-required forms; and

iii. Fees associated with entities that develop systems or lending platforms to automate the CDC's internal loan decision making process, including but not limited to the use of basic credit algorithms or data-based scoring/models where the CDC inputs Applicant data in order to determine creditworthiness.

Note: SBA does not consider entities providing technology services that do not include underwriting to be Agents. Entities providing technology services that include underwriting are considered to be professional services contractors and must be providing their services to the CDC under an SBA-approved professional services contract. See Paragraph E.6.a, Professional Services Contractors, in this Chapter for more information.

4. Use of Agents in the 504 Loan Program

SBA expects CDCs to exercise due diligence and prudent oversight of their third party vendors, including professional service contractors and other loan agents, which should include having written policies governing such relationships and monitoring performance of loans referred by an Agent or where an Agent provided assistance. SBA will review evidence of such due diligence and oversight of such relationships when conducting CDC oversight activities.

SBA regulations at 13 CFR Part 103 govern the activities of Agents, the disclosure of fees, and the circumstances that would result in revocation or suspension of the Agent's privilege to conduct business with SBA.

In 13 CFR § 103.1(a), SBA defines an "Agent" to mean an authorized representative, including an attorney, accountant, consultant, packager, lender service provider, or any other person representing an Applicant or participant by Conducting Business with SBA. Note: The term Agent in 13 CFR § 103.1(a) includes Lender Service Providers, which are used only in the 7(a) Loan Program. Professional Services Contractors are used in the 504 Loan Program and are described in Paragraph 5. below.

a. For individuals or entities operating under a professional services contract with a CDC, SBA approves the written agreement or contract with the CDC and the SBA Form 159 is not required. (13 CFR §§ 103.5(c) and 120.824) (Professional Services Contracts are used under the 504 Program rather than Lender Service Provider Agreements. See Paragraph 6 Professional Services Contractors, below, for guidance on professional service contracts.) Fees paid by the CDC in accordance with the professional services contract cannot be passed onto the Applicant.

b. For all other Agents, paid by either an Applicant or a CDC, an SBA Form 159 must be completed and signed by the Applicant, the CDC, and the Agent. See Paragraph 6. Disclosure of Fees – SBA Form 159, below, for more information on SBA Form 159.

**c.** The only situation where an Agent can receive compensation from both the CDC and the Applicant is when the Agent is providing different services by providing packaging services to the Applicant and receiving a referral fee from the CDC.

d. The SBA does not allow contingency fees (fees paid only if the loan is approved or closed) or charges for services which are not reasonably necessary in connection with an application.

e. The Director of SBA's Office of Credit Risk Management (D/OCRM) may, for good cause, suspend or revoke the privilege of an Agent to conduct business with the government. The suspension or revocation will remain in effect during any administrative proceedings under SBA regulations at 13 CFR Part 134. The meaning of "good cause" can be found at 13 CFR § 103.4.

f. Agents and Privacy Act Considerations:

Private information about a loan cannot be discussed with anyone who claims to be an Agent for an Applicant or CDC without evidence of representation. Proprietary information is protected by the Right to Financial Privacy Act and the Privacy Act. Without proper authorization, SBA and CDCs may not discuss private information with even a spouse or other close relative of the Applicant. SBA may require that an Agent supply written evidence of their authority to act on behalf of an applicant

or CDC as a condition of revealing any information about the applicant's or CDC's current or prior dealings with the SBA.

5. Fees an Agent May Charge an Applicant for Packaging and Other Services

   CDCs and Agents must clearly inform any Applicant in writing that the SBA does not require the use of an Agent for packaging or referring a loan application.

   a. An Agent may charge an Applicant for:

      i. Packaging services to assist the Applicant with completing one or more applications, preparing a business plan, cash flow projections, and other documents related to the application; and

      ii. Other services that include consulting as to the amount and type of financing needed and broker or referral fees.

   b. The fees must be reasonable and customary for the services actually performed.

   c. An Agent may charge an Applicant fees for packaging and other services based on an hourly rate or on a percentage of the loan amount. In either case, all fees over $2,500 must be supported by documenting the service performed.

   d. For fees charged to an Applicant on an hourly rate, there is no maximum, but the fees must be reasonable and customary for the services actually performed. The hourly rate and time spent on each service must be documented.

   e. For fees charged to an Applicant based on a percentage of the loan amount, the fee may not exceed (if multiple services are provided to the Applicant, the combined fee for all services cannot exceed the stated maximums below):

      i. 3 percent on loans of $50,000 or less;

      ii. 2 percent for loans between $50,000 and the first $1,000,000 and 0.25 percent on the portion over $1,000,000; however,

      iii. The maximum fee that may be charged in the aggregate to an Applicant on a percentage basis is $30,000.

   **f.** If an Agent or Agents charge an Applicant fees in connection with obtaining a 504 loan, the Agent(s) must disclose the fees to SBA by completing SBA Form 159 in accordance with Paragraph E.7 below.

   g. SBA does not allow an Agent to charge an Applicant:

      i. A standard or flat fee charged to all Applicants;

      ii. Contingency fees (fees paid only if the loan is approved or closed); or

      iii. For services that are not reasonably necessary in connection with an application.

h. SBA may review these fees at any time. Agents must refund any fee considered unreasonable or impermissible by SBA.

i. Review of Agent Fees:

i. CDCs must review the Agent's services and related fees to determine if the fees are necessary and reasonable when:

a) There is an indication from a third party that an Agent's fees might be excessive; or

b) When an Applicant complains about the fees charged by an Agent.

ii. In cases where fees appear to be unreasonable, CDCs should contact the D/OCRM to report the fees.

**iii.** If an SBA investigation determines an Agent fee is excessive, the Agent must reduce the fee to an amount SBA deems reasonable, refund any sum in excess of that amount to the Applicant, and refrain from charging or collecting from the Applicant any funds in excess of the amount SBA deems reasonable.

6. Professional Services Contractors

13 CFR § 120.824

a. Pre-approval of a professional services contract by the D/FA is required prior to engaging the services of a contractor for any of the following functions:

- Managing (a request for a waiver of the requirement that the manager be employed directly by the CDC must be submitted to SBA;
- Marketing;
- Packaging;
- Processing;
- Closing;
- Servicing;
- Liquidating;
- Legal services in connection with loan liquidation or litigation;
- Independent Loan Reviews to be conducted by another CDC. CDCs may not review each other's portfolios or exchange any other services, nor may they enter into any other arrangement with each other that could appear to bias the outcome or integrity of the independent loan review; or
- Co-employment contracts (e.g., for paying wages and taxes and providing retirement and health benefits to the CDC's staff under which the CDC and the contractor are deemed to be co-employers of the CDC's staff).

b. CDCs may contract for the following functions without SBA approval:
   - Accounting;
   - Legal services (except in connection with loan liquidation or litigation);
   - Information technology; and
   - Independent loan review services performed by a non-CDC.

c. CDCs entering into a contract to provide services to another CDC:
   i. Must be located in the same SBA Region (except for contracts for liquidation services or independent loan reviews); or
   ii. If not located in the same SBA Region, must be located in a contiguous State (except for contracts for liquidation services or independent loan reviews); and
   iii. May provide assistance to only one CDC per State (except for contracts for liquidation services or independent loan reviews);
   iv. Must not provide assistance to another CDC in its State of Incorporation or any State in which the CDC has multi-state authority (except for contracts for liquidation services or independent loan reviews);
   v. Must have a separate and independent Board of Directors;
   vi. If either CDC is for-profit, neither may own stock in the other CDC;
   vii. CDCs are prohibited from comingling any funds.
   viii. Notwithstanding the prohibition in 13 CFR § 120.820(d) against a CDC affiliating with another CDC, a CDC may, with SBA's prior written approval, obtain services through a contract with another CDC even if the arrangement would give rise to an affiliation between the CDCs based on an "identity of interest," as defined under 13 CFR § 121.103(f). However, affiliation between CDCs based on grounds other than identify of interest, including but not limited to, through ownership or common management under 13 CFR § 121.103(c) and (e), respectively, would continue to be prohibited.

d. Review and Pre-Approval:
   i. For all contracts that require prior approval (except for contracts involving legal services in connection with loan liquidation or litigation), the 504 Loan Program Division reviews the contracts and provides its recommendation to the D/FA, or designee, who makes the final decision.
   ii. With respect to contracts for management or independent loan reviews performed by another CDC, the D/FA's final decision will be made in consultation with the D/OCRM (or designee).

iii. The Office of Financial Assistance (OFA) will notify the CDC in writing of the D/FA's final decision and will provide a copy of the decision to the Lead District Office.

iv. For contracts involving legal services in connection with loan liquidation or litigation, the appropriate Commercial Loan Servicing Center will review and approve the contracts.

v. If a CDC engages the services of a contractor without obtaining SBA's approval in accordance with the process described below, the CDC's non-compliance will be reported to OCRM. In addition to any other appropriate action, any loan application requests sent to the SLPC by an individual employed under the contract may be delayed for processing and approval until such time as the professional services contract is approved by the D/FA.

e. Submission Process:

i. At least 60 days prior to the date on which the CDC intends to engage the contractor's services, the CDC must submit to OFA at 504Requests@sba.gov:

a) A request from a responsible CDC management official to review the draft materials;

b) An unsigned draft of the contract; and

c) A justification from the CDC's Board of Directors explaining its reasoning for why the Board believes it is in the best interest of the CDC to contract for CDC functions. (13 CFR § 120.824(a)).

ii. The request for SBA's approval of a contract may not be submitted with the CDC's Annual Report. (The Annual Report must include a list of all CDC contracts by status (e.g., current, not current, expired) with renewal dates and/or expiration dates.)

iii. If the D/FA approves the contract, the CDC must submit a copy of the fully executed contract to OFA upon its execution by the parties.

iv. If the CDC wishes to renew a professional services contract, the CDC must re-submit the contract at least 60 days prior to the end of the approved contract term (including any approved optional renewal years) for review and pre-approval.

f. The professional services contract:

i. Must state the following:

a) The CDC's Board of Directors specifically acknowledges and retains the ultimate responsibility for all loan approvals and loan servicing actions, and that such responsibility must be carried out independently of any control by the contractor, 13 CFR §120.823;

b) No contractor or any officer, director, 20 percent or more equity owner, or Key Employee of a contractor may be a voting or non-voting member of the CDC's Board of Directors;

c) All compensation paid to the contractor will be paid by the CDC and the contractor cannot charge the Borrower for the same services; and

d) The contractor is prohibited from requiring a 504 Applicant or Borrower to purchase other services from the contractor as a condition of the contractor's performing CDC staff or management functions;

e) Each individual performing services must receive a character determination.

f) CDCs are responsible for the actions of their contractors and must ensure that they comply with all applicable laws and regulations governing confidentiality. CDCs should consult with their Counsel to obtain appropriate language to be included in the contracts.

ii. Must include the following:

a) A description of services that the contractor will perform;

b) A description (resume or summary of work history/relevant experience) of each individual providing services under the contract;

c) A breakdown of compensation by individual if more than one person is being compensated under the contract;

d) The rate of compensation for all parts of the contract except servicing stated at an hourly rate (the servicing portion may be based on a percentage not to exceed the amount authorized by the regulations 13 CFR §120.971(a)(3));

e) The basis for its determination that the fees are customary and reasonable for similar services in the area;

f) A statement that additional compensation from CDC fee income such as multipliers or bonuses is not permitted;

g) A provision that allows the CDC procuring the services to terminate the contract with written notice (usually a 30 to 60 day notice) without penalty and with or without cause at any time prior to the expiration date of the contract;

iii. Must not:

a) Include any contractual services provided by the Executive Director of a CDC;

b) Evidence any actual or apparent conflict of interest or self-dealing on the part of any of the CDC's officers, management, and staff, including any members of the Board or any Loan Committee;

c) Diminish the responsibility of the Board of Directors for the operations of the CDC;

iv. Must be accompanied by a Board of Directors' Resolution containing the following statements:

a) The contract is in compliance with 13 CFR §§ 120.823, 120.824 and 120.825 and SBA Loan Program Requirements;

b) Of understanding that the contract is subject to pre-approval by SBA D/FA upon each new contract term; and

c) Of understanding that approved contracts are subject to yearly review by SBA.

7. Disclosure of Fees – SBA Form 159

Section 13 of the Small Business Act (15 U.S.C. § 642) requires that an Applicant identify the names of Persons (as defined in 13 CFR § 120.10) engaged by or acting on behalf of the Applicant for the purpose of expediting the application and the fees paid or to be paid to any such Person. SBA regulations at 13 CFR § 103.5 require the Applicant, CDC, and any Agent to execute and provide to SBA a compensation agreement ("Agreement"). Each Agreement governs the compensation charged for services rendered or to be rendered to the Applicant or CDC in any matter involving SBA assistance.

a. CDCs must identify in the SBA Loan System whether an Agent was involved in any way with the transaction and provide the name, street address, city, state, and zip code of the Agent. For Applications involving an Agent, SBA Form 159 can be generated using the SBA Loan System.

b. For Agents other than professional services contractors performing duties for the CDC under an SBA-approved professional services contract, if the Agent is paid by an Applicant or CDC, an SBA Form 159 must be completed in accordance with form instructions and signed by the Applicant, the Agent, and the CDC. Do not report fees paid for the Third Party Lender's loan on SBA Form 159. Separate SBA Forms 159 must be completed for each Agent who provides services to the Applicant. Failure of an Agent to fully complete and execute the required SBA Form 159 may result in suspension or revocation of the Agent's privilege to conduct business with SBA under 13 CFR Part 103.

c. SBA Form 159 "Fee Disclosure Form and Compensation Agreement"

i. Information on this form will be used to monitor fees charged by Agents and the relationship between Agents and CDCs. CDCs must complete all

appropriate data fields on SBA Form 159 in accordance with the form instructions. For example, the seven-digit FIRS number must be included exactly as assigned by SBA and without any extra characters.

ii. If the aggregate compensation for all fees provided by the same Agent exceeds $2,500, the compensation must be itemized.

a) When an Agent charges an Applicant in connection with multiple applications (for example, an Applicant is seeking a 504 loan and a 7(a) loan):

i) Separate SBA Forms 159 must be completed for each application and for each Agent.

ii) Fees are aggregated to establish the $2,500 threshold for itemization.

b) When the Agent provides multiple services (for example, an Agent is providing both loan packaging and referral services to the Applicant), each service must be separately reported on the same SBA Form 159. For example:

i) In the "Type of Agent" section, select both the "Independent Loan Packager" and the "Referral Agent/Broker" boxes; and

ii) In the "Type of Service" table, separately itemize the amounts paid in each appropriate box.

c) In-kind compensation (i.e., non-monetary contributions for goods or services) paid or to be paid by the CDC must be itemized.

iii. The following are not considered Agents for purposes of this Agreement and are not required to complete SBA Form 159:

a) Applicant's accountant for the preparation of financial statements required by the Applicant in the normal course of business and not related to the loan application;

b) A state-certified or state-licensed appraiser employed by the CDC to appraise collateral in connection with the SBA Loan;

c) A professional services contractor performing services for the CDC under an SBA-approved professional services contract;

d) An environmental professional employed by the CDC to conduct an environmental assessment of the collateral in connection with the SBA Loan;

e) Any attorney in connection with the SBA Loan closing; and

f) A real estate agent who is receiving a commission for the sale of real estate in connection with the SBA Loan.

iv. CDCs must upload a copy of the completed SBA Form 159, signed by all applicable parties, along with any required supporting documentation into the Corporate Governance Repository within 30 calendar days after the debenture funds. The CDC must provide a list of all SBA Form 159 submissions in the Annual Report (SBA Form 1253) for the fiscal year. A separate Form 159 must be completed for each application when an Agent provides services to an Applicant in connection with multiple applications. CDCs are required to retain an original signature version of the form and all supporting documentation in their files for compliance review purposes.

# CHAPTER 5: OTHER CORE REQUIREMENTS

## A. GUARANTIES

13 CFR § 120.160(a)

Each loan must be guaranteed by at least one individual or entity. If no one individual or entity is a direct and/or indirect owner of 20% or more of the Applicant, at least one of the owners must provide a full unconditional guaranty. In addition, if the guaranty will be provided by a trust, the requirements of Paragraph 3, Corporate/Other Guaranties below must be met.

1. Personal Guaranties:
    a. Any individual who has direct and/or indirect ownership of 20% or more of an Applicant must provide an unlimited full guaranty. (SBA Form 148 or, for 7(a) loans, equivalent Lender's form). If a person has executed the Note as a Borrower in an individual capacity, that person does not also have to execute a personal guaranty.
    b. When ownership interest of an Applicant is held by a corporation, partnership or other form of legal entity, the ownership interests of all individuals must be disclosed.
    c. When deemed necessary for credit or other reasons, SBA or, for a loan processed on a delegated basis, the SBA Lender, may require other appropriate individuals or entities to provide full or limited guaranties of the loan without regard to the percentage of their ownership interests, if any. For example, an individual with a minority ownership or no ownership interest in the Applicant or OC who is critical to the operation of the business may be required to provide a personal guaranty (e.g., Supplemental Guarantors).
    d. If a limited guaranty is used, the SBA Lender must choose one of the payment limitation options in SBA Form 148L (Unconditional Limited Guaranty) or, for 7(a) loans, equivalent Lender's form and specify the option in the SBA Terms and Conditions.
    e. The SBA Lender must obtain a personal financial statement from all individuals guaranteeing the loan except for Supplemental Guarantors, dated within 90 days of loan approval.
    f. Guarantors must comply with the requirements in Ch. 1, Para. F, Citizenship and Residency Requirements.
2. Guaranty of Spouse:

a. Each spouse owning less than 20% of an Applicant must personally guarantee the loan in full when the combined ownership interest of both spouses and minor children is 20% or more.

b. For a non-owner spouse, the SBA Lender must require the signature of the spouse on the appropriate collateral documents. Non-owner spouses are not required to sign the personal financial statement. The spouse's guaranty secured by jointly held collateral will be limited to the spouse's interest in the collateral.

c. Guarantors must comply with the requirements in Ch. 1, Para. F, Citizenship and Residency Requirements.

3. Corporate/Other Guaranties:

a. All entities that have direct and/or indirect ownership of 20% or more of an Applicant must provide an unlimited full guaranty. If the entity that owns any percentage of the Applicant is a trust (revocable or irrevocable), the trust must guarantee the loan with the trustee executing the guaranty on behalf of the trust and providing the certifications required in Section A, Ch 2, Para. A.2., Conditions that apply when the EPC is owned in whole or in part by a trust. In addition, the Trustor must also personally guarantee the loan.

b. The SBA Lender must obtain appropriate financial statements from all entities guaranteeing the loan in order to determine the assets available to support the guaranty.

c. When deemed necessary for credit or other reasons, SBA or, for a loan processed on a delegated basis, the SBA Lender, may require other appropriate entities to provide full or limited guaranties of the loan without regard to the percentage of their ownership interests, if any. This may include entities who manage the day-to-day operations of the Applicant or OC through a Management Agreement without an ownership interest in the Applicant or OC.

4. Reducing Ownership Interest (Six-month lookback rule):

a. Any Person (as defined in 13 CFR 120.10) subject to the guaranty requirements 6 months prior to the date of the loan application would continue to be subject to the requirements even if that Person has changed their ownership interest to less than 20%. Except for Ineligible Persons covered under Ch. 1, Para. F, Citizenship and Residency Requirements.

b. Exceptions to the 6-month lookback rule:

i. When that Person completely divests their interest prior to the date of application. Complete divestiture includes divestiture of all ownership interest and severance of any relationship with the Applicant (and any associated Eligible Passive Company) in any capacity, including being an employee (paid or unpaid), for the life of the 7(a) or 504 loan.

ii. For 7(a) loans for partial changes of ownership, the percentages of ownership for determining who must provide a guaranty will be based on the post-sale percentage of direct and/or indirect ownership in the business. See the appropriate sections in this SOP on partial changes of ownership for more information.

## B. IRS TAX TRANSCRIPT/VERIFICATION OF FINANCIAL INFORMATION

1. The purpose of SBA's Tax Verification process is to determine if:
    a. The Applicant filed business tax returns; and
    b. The Applicant's financial statements provided as part of the application agree with the business tax returns submitted to the IRS.
2. If an Applicant has not filed required Federal tax returns, the Applicant is not eligible for SBA financial assistance.
3. For a sole proprietorship, the SBA Lender must verify the Schedule C. For a change of ownership, the SBA Lender must verify the seller's financial data, including a selling sole proprietor's Schedule C, except when there is an acquisition of a division or a segment of an existing business, the SBA Lender may use alternative forms of third-party verification such as third-party CPA-prepared or reviewed financial statements, sales tax payment records, transient occupancy tax, credit reporting services, etc., to verify the seller's financial data.
4. Except for the SBA Express and Export Express Programs, SBA Lenders must obtain tax return transcripts and reconcile any discrepancies with the Applicant's financial data against the tax transcripts, for 7(a), prior to first disbursement of loan proceeds, or for 504, prior to submitting the request to fund the debenture:
    a. If the Applicant is determining eligibility under the SBA size requirements using the:
        i. NAICS Size Standard: For the Applicant, or the Operating Company if the Applicant is an EPC, for the last 3 years, (unless Applicant or Operating Company is a Start-Up Business). If the business has been operating for less than 3 years, the SBA Lender must obtain the information for all years in operation.
        ii. Alternative Size Standard: For the Applicant, or the Operating Company if the Applicant is an EPC, for the last 2 years. If the business has been operating for less than 2 years, the SBA Lender must obtain the information for all years in operation.
        iii. The requirements in i. and ii. above does not include tax information for the most recent fiscal year if the fiscal year-end is within 6 months of the date SBA received the application. If the Applicant has filed an extension for the

most recent fiscal year, the SBA Lender must obtain a copy of the extension along with evidence of payment of estimated taxes.

b. SBA Lenders may obtain tax transcripts through either of the following methods:

   i. Through the IRS's Income Verification Express Service (IVES) program: SBA Lenders may either enroll in IVES or contract with an IVES participant. Additional information on IVES enrollment is available at www.irs.gov/individuals/ives-enrollment-procedures. Or;

   ii. By fully completing and submitting IRS Form 8821:

      a) SBA Lenders must ensure the type of transcript requested contains any changes to the original return.

      b) The SBA Lender must be listed as designee on line 2 of IRS Form 8821. If the SBA Lender uses an LSP for the application, both the SBA Lender and the LSP must be listed as designees on line 2 of IRS Form 8821.

      c) SBA will not permit the borrower or its own tax preparer or enrolled agent to file IRS Form 8821 for an SBA loan.

c. If the IRS advises that it has no record on the Applicant or no record of any of the required years of transcripts, no disbursements may be made on the loan and either the loan must be canceled, or the closing must be postponed until the issue is resolved unless the SBA Lender can document that the requirements of g. below have been fulfilled.

d. For loans where 3 years of transcripts are required: If the IRS transcript reflects "Record Not Found" for the middle year of the 3 years requested, and the SBA Lender has verified the other 2 years, AND the Applicant has some record of either receiving a refund or paying the taxes for the missing year, then the SBA Lender may reasonably assume that the Applicant filed a return for the missing year. If the SBA Lender documents all these steps in its loan file, the SBA Lender has demonstrated to SBA that it has made a good faith effort to satisfy the verification requirement.

e. If the Applicant has filed an amended return: The Lender must follow all steps in this section to obtain and retain copies of the IRS tax transcript(s), when required. If the amended return transcript is not available from the IRS, the Lender must obtain a copy of the signed amended return for verification of financial records and obtain evidence of filing the amended return. Evidence may include an electronic filing acknowledgement (IRS Acceptance Report), Certified Mail receipt (USPS Form 3800), Certified Mail return receipt, or USPS delivery confirmation, stamped amended return by IRS, or a letter from the Accountant or CPA.

f. If the SBA Lender does not receive a response from the IRS or the copy of the tax transcript within 10 business days, the SBA Lender must follow up with the IRS to

obtain and verify the tax data by resubmitting a copy of IRS Form 4506-C or IRS Form 8821 to IRS with the notation "Second Request" in the top right-hand side. Any significant differences must be resolved to the satisfaction of the SBA Lender, and, if processing the loan under non-delegated procedures, to the SBA loan processing center.

i. For a 7(a) Lender processing a loan under its delegated authority, the Lender may proceed to close and disburse the loan; however, if the Lender disburses the loan and is unable to obtain the tax transcript and, when applicable, reconcile the tax transcript with the financial data provided by the Applicant, the guaranty may be subject to repair or denial;

ii. For a CDC processing a 504 loan under PCLP or ALP Express authority, the CDC may proceed to close and disburse on the interim loan, however, the CDC may not submit the closing package for the debenture sale until the CDC is able to reconcile the IRS information.

g. SBA Express and Export Express Programs:

i. If the Lender uses business financial information to determine the creditworthiness of an SBA Loan, the Lender must follow the IRS tax verification process set out in this section.

ii. If the Lender does not use business financial information to determine creditworthiness, such as with some credit scoring models, Lender must obtain IRS tax transcripts in order to verify that the returns were filed and for the purpose of determining the Applicant's size, but reconciliation of the tax transcripts is not required.

iii. SBA Express and Export Express Lenders are authorized to close and disburse a loan immediately if disbursement is requested by the Borrower; however, Lenders must follow-up and verify the business financial data with IRS tax data and must document the loan file accordingly. If, after loan disbursement, the Lender is unable to obtain the tax transcript and, when applicable, reconcile the tax transcript with the financial data provided by the Applicant, the guaranty may be subject to repair or denial.

h. No records found: When the SBA Lender is unable to obtain a required tax transcript due to the IRS having no record of the return, SBA will permit the SBA Lender to proceed with loan closing if ***both*** of the following have been obtained:

i. Proof of filing of the required tax return, either through evidence of an IRS E-file submission or a paper return that has been stamped as received by the IRS, ***and***

ii. Proof of payment or refund of tax liability that reconciles with the stated liability on the tax return. If the business' tax liability is passed through to

individual guarantors, the SBA Lender may use IRS tax transcripts for the individuals to verify their payment of taxes.

5. Exception for U.S. Territories: For Applicants located in U.S. Territories when the Applicant is not required to file Federal income tax returns, in lieu of obtaining and verifying tax data from the IRS, SBA Lenders must verify the receipt-stamped copies of the income tax returns filed with the territory's taxing authority, as applicable. This exception applies any place in this SOP that references tax transcripts.

## C. INSURANCE REQUIREMENTS

SBA Lenders must ensure all appropriate insurance requirements are included in the SBA Terms and Conditions and SBA Lender's credit memorandum.

1. Hazard Insurance

   13 CFR § 120.160(c)

   a. For 7(a) loans greater than $50,000, and for 504 projects greater than $50,000, SBA requires hazard insurance on all assets pledged as collateral. If hazard insurance is not available, the loan cannot be approved. The Borrower must also maintain a separate policy if the business is located in a state that requires additional coverage such as wind, hail, earthquake, or other. This policy applies to all loans except the following:

      i. For loans of $500,000 or less, if residential real estate is pledged as collateral and the lien will not be in first position, and if hazard insurance cannot be obtained, then it is not required on the residential real estate; and

      ii. For loans of $500,000 or less, if the full replacement value of the business's assets is $50,000 or less.

   b. Real Estate

      i. Coverage must be in the amount of the full replacement cost.

      ii. If full replacement cost insurance is not available, coverage must be for the maximum insurable value.

      iii. Insurance coverage must contain a MORTGAGEE CLAUSE (or substantial equivalent) in favor of the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504),. This clause must provide that any action or failure to act by the mortgagor or owner of the insured property will not invalidate the interest of the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504). The policy or endorsements must provide for at least 10 days prior written notice to the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504), of policy cancellation.

   c. Personal Property

      i. Coverage must be in the amount of full replacement cost.

ii. If full replacement cost insurance is not available, coverage must be for maximum insurable value.

iii. Insurance coverage must contain a LENDER'S LOSS PAYABLE CLAUSE (or substantial equivalent) in favor of the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504). This clause must provide that any action or failure to act by the debtor or owner of the insured property will not invalidate the interest of the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504). The policy or endorsements must provide for at least 10 days prior written notice to the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504), of policy cancellation.

d. Exceptions for SBA Express and Export Express

If the Lender does not require hazard insurance (for example, if it would impose an undue burden on an Applicant given the small size of a loan), the Lender must document the reason in its loan file.

2. Marine Insurance

a. When a vessel(s) is(are) the collateral on the loan, SBA Lender must obtain coverage in the amount of the full insurable value on the vessel(s) with the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504), designated as “Mortgagee”.

b. The policy must contain a Mortgagee clause providing that the interest of the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504), will not be invalidated by any:

i. Act, omission, or negligence of the mortgagor, owner, master, agent, or crew of the vessel;

ii. Failure to comply with any warranty or condition out of mortgagee’s control; or

iii. Change in title, ownership, or management of the vessel.

c. The policy must include Protection and Indemnity, Breach of Warranty, and Pollution coverage.

d. The policy or endorsements must provide for at least 10 days prior written notice of policy cancellation to the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504).

3. Flood Insurance

a. SBA flood insurance requirements are based on the Standard Flood Hazard Determination (FEMA Form 086-0-32 or its successor). The mandatory purchase of flood insurance will be required as set forth by the provisions of the National Flood Insurance Program (NFIP) and the Interagency Questions and Answers Regarding Flood Insurance at 12 CFR Part 22, 12 CFR Part 208, 12 CFR Part 339, 12 CFR Part 614 and 12 CFR Part 760. Policies for condominium and cooperative units will consist of a policy obtained by the individual unit owner for the

particular unit. For 504, CDCs must obtain a FEMA Form 086-0-32 (or its successor), or a copy of the form obtained by the Interim or Third Party Lender.

b. Private flood insurance will be accepted; however, it must meet the same requirements as the standard NFIP policy. If used, private flood insurance must:

   i. Provide coverage that is at least as broad as the coverage provided under the standard NFIP policy, including when considering deductibles, exclusions, and conditions offered by the insurer;

   ii. Include an endorsement that the insurer must give 45 days' notice of cancellation for non-renewal to the insured and the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504);

   iii. Include information about the availability of flood insurance coverage under the NFIP;

   iv. Contain a mortgage interest clause similar to the one in the standard NFIP policy;

   v. Contain a provision requiring an insured to file suit not later than 1 year after date of a written denial of all or part of a claim under the policy; and

   vi. Contain cancellation provisions that are as restrictive as the provisions contained in the standard NFIP policy.

c. If any portion of a building that is collateral for the loan is located in a special flood hazard area, the SBA Lender must require the Applicant to obtain flood insurance for the building under the NFIP or comparable private flood insurance (see Subparagraph b above).

d. If any equipment, fixtures or inventory that is collateral for the loan ("Personal Property Collateral") is in a building of which any portion is located in a special flood hazard area and that building is collateral for the loan, SBA Lender must require Applicant to also obtain flood insurance for the Personal Property Collateral either under the NFIP or through comparable private flood insurance (see Subparagraph b above).

e. Insurance coverage must be at least equal to the outstanding principal balance of the loan or the maximum limit of coverage made available under the National Flood Insurance Act of 1968, as amended (42 U.S.C. § 4001 et seq.), whichever is less. ("Maximum limit of coverage available" is the lesser of the maximum limit available under the NFIP for the type of structure or the insurable value of the structure.)

f. Insurance coverage must contain a MORTGAGEE CLAUSE/LENDER'S LOSS PAYABLE CLAUSE (or substantial equivalent) in favor of the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504). This clause must provide that any action or

failure to act by the debtor or owner of the insured property will not invalidate the interest of the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504). The policy or endorsements must provide for at least 10 days prior written notice of policy cancellation to the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504), or 45 days in the case of private flood insurance.

4. Life Insurance

   a. If the SBA Lender determines that the principal is uninsurable, the SBA Lender must obtain written documentation from a licensed insurer of the same.

   b. For each policy required under this Paragraph, SBA Lenders must obtain a collateral assignment identifying the 7(a) Lender (for 7(a)), or the CDC/SBA (for 504), as assignee that is acknowledged by the Home Office of the Insurer. SBA Lenders must ensure that the Applicant/Borrower pays the premiums on the policy (13 CFR § 120.970(c)).

   c. SBA Lenders may accept the pledge of an existing life insurance policy. Credit life insurance or whole life insurance should not be required.

   d. 7(a) Loans

      i. For Standard 7(a), EWCP, CAPLines, International Trade loans and pilot programs (unless specified otherwise in the pilot program guide), 7(a) Lenders may follow their internal policy for similarly-sized non-SBA guaranteed commercial loans. If the loan is not fully secured, life insurance is required in the amount of the collateral shortfall for the principals of sole proprietorships, single member LLCs, or for businesses otherwise dependent on one owner's active participation.

      ii. For 7(a) Small Loans, SBA Express and Export Express loans, SBA Lenders may follow their internal written policy for their similarly-sized, non-SBA guaranteed commercial loans.

   e. 504 Loans

      CDCs must assess whether the viability of the business is tied to an individual or individuals. Life insurance is required for the principals of sole proprietorships, single member LLCs, or for businesses otherwise dependent on one owner's active participation when the SBA Loan is not fully collateralized.

      i. If the CDC determines the principal is uninsurable, the CDC must obtain written documentation from a licensed insurer of the same.

      ii. For each policy required under this Paragraph, CDCs must obtain a collateral assignment identifying the CDC/SBA as assignee that is acknowledged by the Home Office of the Insurer. CDCs must ensure that the Applicant/Borrower pays the premiums on the policy (13 CFR § 120.970(c)).

iii. CDC may accept the pledge of an existing life insurance policy. Credit life insurance or whole life insurance should not be required.

iv. When required, the minimum term of life insurance is:

a) 10 years for a 10 year debenture.

b) 20 years for a 20 or 25 year debenture.

v. For the purpose of life insurance calculation, the loan is considered fully collateralized when the value of the discounted collateral is equal to or greater than the net debenture amount. When the loan is not fully collateralized, the amount of life insurance required is equal to the difference between the net debenture amount and the value of the discounted collateral.

vi. For life insurance only, the calculation of discounted collateral is as follows:

a) Improved real estate at 85% of fair market value determined in accordance with the appraisal requirements in Section C, Ch. 1, Para. E.2.b., Appraisals.

b) New machinery and equipment (excluding furniture and fixtures) at 75% of price minus any prior liens.

c) Used or existing machinery and equipment (excluding furniture and fixtures) at a maximum of 50% of Net Book Value or 80% with an Orderly Liquidation Appraisal minus any prior liens.

## D. HISTORIC PROPERTIES

Section 106 of the National Historic Preservation Act requires Federal agencies to consider whether their federally-funded projects directly or indirectly adversely impact properties and sites that are listed or eligible to be listed on the National Register of Historic Places (NRHP). (54 U.S.C. § 300101 et seq.; 36 CFR §§ 60.1 et seq. and 800.1 et seq.) An SBA Loan is considered to directly or indirectly impact such a property or site if the SBA Loan transaction involves the purchase or renovation of a property or site (including installation of equipment). As set forth below, SBA will conduct a Section 106 review to determine whether the impact is adverse.

For all SBA Loan transactions involving the purchase or renovation of a property or site (including installation of equipment), all SBA Lenders must conduct due diligence to determine whether the SBA Loan transaction involves a property or site that is listed on the NRHP or has historic significance such that it may be eligible to be listed on the NRHP (either individually or as part of a historic district). The due diligence conducted must follow prudent lending practices and be documented in the SBA Loan file. Each loan application must be individually reviewed. For example, if a 7(a) loan is made a short time after a 504 loan, the 7(a) loan must have an individual review.

1. If the SBA Lender's due diligence does not yield information indicating that the property or site is listed on the NRHP or has historic significance such that it may be eligible to be listed on the NRHP (either individually or as part of a historic district), the SBA Lender must document its file and does not need to request a Section 106 review by local SBA counsel. However, the SBA Lender may request a Section 106 review by local SBA counsel if it subsequently receives a screen out notice from the SBA loan processing center.
2. If the SBA Lender's due diligence yields information indicating that the property or site is listed on the NRHP or has historic significance such that it may be eligible to be listed on the NRHP (either individually or as part of a historic district), the SBA Lender must take the following actions:
    a. For SBA Loan transactions involving property or site acquisition where the Borrower, Co-Borrower, and/or Operating Company has no intention of altering, renovating, rehabilitating, restoring, and/or demolishing any part of the property or site:
        i. Prior to submitting the SBA Loan application to the SBA loan processing center (non-delegated) or requesting an SBA Loan Number when processing the SBA Loan under delegated authority, the SBA Lender must obtain a Historic Property Borrower Certification executed by the Borrower, Co-Borrower, and/or Operating Company. This is a self-certification that no modifications will be made to the property or site during the term of the SBA Loan. This self-certification must be made on SBA Form 2481, Historic Property Borrower Certification.
        ii. The SBA Lender must provide a copy of the executed SBA Form 2481 to local SBA counsel for review and clearance. This clearance will become null and void and a Section 106 review will be required if, between the date the SBA Form 2481 is executed and the date the SBA Loan is disbursed, the Borrower, Co-Borrower, and/or Operating Company changes its intentions or it is determined the property or site requires any alteration, addition, renovation, rehabilitation, restoration, and/or demolition.
        iii. SBA Lenders processing the loan under their delegated authority must retain the executed SBA Form 2481 and clearance from local SBA counsel in the SBA Loan file. The executed SBA Form 2481 and clearance from local SBA counsel must be provided with any guaranty purchase request and may be reviewed by SBA when conducting lender oversight activities.
        iv. SBA Lenders processing the loan under non-delegated procedures must include the executed SBA Form 2481 and clearance from local SBA counsel with the application for review by the SBA loan processing center.

b. For SBA Loan transactions where the Borrower, Co-Borrower, and/or Operating Company intends to alter, renovate, rehabilitate, restore, and/or demolish any part of the property or site (regardless of the source of the funds to finance these modifications), the SBA Lender must request a Section 106 review by local SBA counsel.

   i. In its request for a Section 106 review to local SBA counsel, the SBA Lender must provide:

      a) The names of the Borrower, Co-Borrower, and/or Operating Company;

      b) The SBA Loan Name;

      c) The results of its due diligence;

      d) A full and complete description of the planned modifications; and

      e) A statement regarding whether any of the planned modifications have commenced. If so, SBA Lender must instruct the Borrower, Co-Borrower, and/or Operating Company to stop work, otherwise the SBA Loan may not be approved and/or disbursed.

      f) If the Borrower, Co-Borrower, and/or Operating Company is under contract for the purchase of the property or site and the seller will not agree to extend the closing deadline to accommodate the Section 106 review process or other extenuating circumstances exist that would cause a hardship if the loan is not approved by SBA until after the completion of the Section 106 review process, the SBA Lender may identify these circumstances in the request. Depending upon the circumstances, SBA may exercise its discretion to issue the SBA Terms and Conditions with a Section 106 review condition consisting of the following or similar language: “Historic Property / Section 106 Review: Pursuant to section 106 of the National Historic Preservation Act and its implementing regulations, prior to the SBA Loan closing and the commencement of any renovations, modifications, or repairs to the Property, Borrower, Co-Borrower, and Operating Company (if applicable) must obtain a historic property review clearance from SBA.”

   ii. Local SBA counsel will review the request and may request additional information from the SBA Lender to facilitate the review.

      a) If local SBA counsel determines during the review that the property or site is not listed on the NRHP and is not eligible to be listed on the NRHP because the property or site does not have any historic significance, local SBA counsel will provide a response to the SBA Lender indicating that a Section 106 review is not required. The response

must be retained in the SBA Loan file and may be requested by the SBA loan processing center during application processing.

b) If local SBA counsel determines during the review that the property or site is listed on the NRHP or may be eligible to be listed on the NRHP because the property or site has historic significance, and the modifications to the property or site have already commenced, local SBA counsel must perform a Section 110(k) review before proceeding with a Section 106 review under 54 U.S.C. § 306113 and 36 CFR. § 800.9(c). If the modifications to the property or site have not yet commenced, local SBA counsel is not required to perform a section 110(k) review and instead will proceed directly to the Section 106 review.

c) If local SBA counsel determines during the review that the property or site is listed on the NRHP or may be eligible to be listed on the NRHP because the property or site has historic significance, local SBA counsel will perform a Section 106 review following the procedures set forth in 36 CFR § 800.4 et seq.

   i) Among other things, the Section 106 review will involve evaluation of the property or site under the NRHP criteria (located at 36 CFR § 60.4) and consultation with the relevant State Historic Preservation Office (SHPO) regarding the historic significance of the property or site and whether the planned modifications will adversely affect the property or site, including any associated historic district.

   ii) Depending upon the nature of the review, consultation with additional parties (e.g., Native American Tribes, Native Hawaiian Organizations, local governments) may be required by 36 CFR § 800.4(d)(2).

   iii) Pursuant to 36 CFR § 800.4(d), the SHPO has thirty (30) days to provide a response to local SBA counsel. The SHPO's response may consist of a statement of no objection or concurrence with SBA's determination; an objection to SBA's determination; or a request for additional information.

   iv) After receiving the SHPO's response, local SBA counsel will consult with the Associate General Counsel for Litigation or designee and advise the SBA Lender of the next steps in the review.

d) If consultation with the SHPO results in a determination that the property or site does not satisfy the NRHP criteria, or that the property or site satisfies the NRHP criteria but there will not be an adverse effect, local SBA counsel will consult with the Associate General Counsel for Litigation or designee and if no other historic property concerns exist, will receive an approval indicating that the SBA Loan transaction may

proceed and will issue a Section 106 review clearance to the SBA Lender.

e) SBA Lenders processing the loan under their delegated authority must retain the clearance from local SBA counsel in the SBA Loan file. The clearance must be provided with any guaranty purchase request and may be reviewed by SBA when conducting lender oversight activities.

f) SBA Lenders processing the loan under non-delegated procedures must include the clearance from local SBA counsel with the application for review by the SBA loan processing center.

g) If consultation with the SHPO results in a determination that the property or site satisfies the NRHP criteria and there will be an adverse effect, SBA must further consult with SHPO and, depending upon the review, other parties to resolve the adverse effect. This may result in a Memorandum of Agreement between SBA and SHPO, and other parties as applicable, regarding the resolution of the adverse effect.

## E. ENVIRONMENTAL POLICIES AND PROCEDURES

SBA's environmental policies and procedures apply to all SBA Lenders on all 7(a) and 504 loan programs, except where otherwise indicated. For 7(a) loans, failure to comply with the provisions of this paragraph may result in a denial of SBA's guaranty. Prudent lending practices may dictate additional Environmental Investigations or safeguards.

Definitions: Terms that are capitalized in this Paragraph are defined in Appendix 4.

1. Environmental Contamination Risks

   The risks of environmental Contamination include:

   a. The costs of Remediation could impair the Borrower's ability to repay the loan and/or continue to operate the business;

   b. The value and marketability of the Property could be diminished. If the Borrower defaults, the SBA Lender or SBA might have to abandon the Property to avoid liability or accept a reduced price for the Property;

   c. The SBA Lender or SBA could be liable for environmental clean-up costs and third-party damage claims arising from Contamination if title to contaminated Property is taken as a result of foreclosure proceedings and/or the SBA Lender or SBA exercises operational control at the Property; and

   d. If a Governmental Entity cleans a site, it may be able to file a lien for recovery of its costs which may be superior to SBA's lien.

2. Environmental Investigations

SBA requires an Environmental Investigation of all commercial Property upon which a security interest such as a mortgage, deed of trust, or leasehold deed of trust is offered as security for a loan or debenture. The type and depth of an Environmental Investigation to be performed varies with the risks of Contamination. This paragraph provides minimum standards. Prudent lending practices and internal lending policy may dictate additional Environmental Investigations or safeguards.

3. Submission of Environmental Investigation Reports

Environmental Investigation Reports must be dated within one year of the date of issuance of the SBA loan number. SBA Lenders processing delegated, 7(a) Small Loans, SBA Express and Export Express loans are not required to submit Environmental Investigation Reports via the SBA Loan System, but they must keep a copy of any Environmental Investigation Report in the loan file. All SBA Lenders must comply with and meet the requirements of the Environmental Policies and Procedures as set forth in this SOP. For example, all Transaction Screens, Phase I and Phase II ESAs ***must*** be performed by an Environmental Professional and be accompanied by the Reliance Letter in Appendix 5. (A Reliance Letter is required even if the Environmental Investigation Report is addressed to the SBA Lender.) Any request for an exception to SBA's Environmental Policies and Procedures must be directed to the Environmental Committee, regardless of the method of processing used for the loan. The following process applies ***only*** to loans being processed under non-delegated procedures:

**For Properties With No Contamination:**

Using the Environmental Investigation Steps set forth below, if an Environmental Investigation Report concludes that a Property has No Contamination, it is the SBA Lender's responsibility to certify in the SBA Loan System that the Property complies with all SBA environmental requirements in this SOP, and the SBA Lender must maintain the Environmental Investigation Reports(s) in the SBA Lender's loan file.

**For Properties With Contamination:**

SBA Lenders must use the Environmental Investigation Steps set forth below. If an Environmental Investigation Report reveals Contamination and the SBA Lender still wishes to make the loan, then the SBA Lender must comply with this SOP and must upload all environmental documentation to the SBA via the SBA Loan System. SBA Lenders must then send an e-mail, **without** the environmental reports, to EnvironmentalReviews@sba.gov, which **must** include in the subject line: DISTRICT OFFICE – APPLICATION NUMBER - LOAN NUMBER - LOAN NAME (no spaces in the loan number). Example: "SAN FRANCISCO DISTRICT OFFICE – 98765432 - 1234567810 – ABC CLEANERS". Attorneys in the SBA's Office of General Counsel will respond to SBA Lenders with approval of the environmental submission, request for additional information, etc.

Once the environmental submission is approved, SBA Lenders must keep a copy of the approval e-mail in their loan file. SBA Lenders who believe that an environmental decision rendered by SBA is inconsistent with the SOP may appeal the decision by forwarding a copy of the decision, along with an explanation of how the determination is perceived to be inconsistent with the SOP to EnvironmentalAppeals@sba.gov. **Lenders seeking to rely solely on 5.d.ix "Other Factor(s)" (below), regardless of whether processing a loan under delegated or non-delegated procedures, must forward the Environmental Investigation Report(s) with a memorandum setting forth their request to EnvironmentalAppeals@sba.gov.**

4. Environmental Investigation Steps

   a. NAICS Codes. For all Property *except* a unit in a Multi-Unit Building, the SBA Lender must begin by making a Good Faith effort to determine the NAICS code(s) for the Property's *current and known prior uses* and compare the NAICS code(s) to the list of environmentally sensitive industries in Appendix 6. For a unit in a Multi-Unit Building, the SBA Lender may proceed directly to Subparagraphs ii. a) and b) of this Paragraph below.

      i. If there is a NAICS code match to an environmentally sensitive industry identified in Appendix 6, the Environmental Investigation must begin with a Phase I, regardless of the amount of the loan.

         If the NAICS code begins with 457 (gas stations with or without convenience stores), the Environmental Investigation must begin with a Phase I and the SBA Lender must also refer to and, if applicable, comply with "Environmental Investigation Requirements for Gas Station Loans" in Appendix 7.

      ii. If there is not a NAICS code match to an environmentally sensitive industry, or if the Property is a unit in a Multi-Unit Building, the SBA Lender must proceed as follows:

         a) If the loan amount is up to and including $250,000, the Environmental Investigation may begin with an Environmental Questionnaire.

         b) If the loan amount is more than $250,000, the Environmental Investigation must, at a minimum, begin with an Environmental Questionnaire and Records Search with Risk Assessment.

   b. Environmental Questionnaire Results. If the Environmental Questionnaire reveals it is unlikely that there is environmental Contamination at the Property and that no further investigation is warranted, the SBA Lender must retain the results of the Environmental Investigation in the SBA Lender's file.

If at any time an Environmental Questionnaire reveals that further investigation is warranted, the SBA Lender must obtain, at a minimum, a Records Search with Risk Assessment.

c. Environmental Questionnaire and Records Search with Risk Assessment Results:

   i. If the Environmental Questionnaire reveals it is unlikely that there is environmental Contamination at the Property and that no further investigation is warranted, and the Records Search with Risk Assessment concludes that the Property is a "low risk" for Contamination, the SBA Lender must keep a copy of the Environmental Questionnaire and the Records Search with Risk Assessment results in the loan file.

   ii. If the Records Search with Risk Assessment concludes that the Property is anything other than "low risk" for Contamination, the SBA Lender must obtain a Phase I ESA.

d. Transaction Screen Results:

   i. If the Environmental Professional conducting the Transaction Screen concludes that no further investigation is warranted, the SBA Lender must keep a copy of the Transaction Screen and review in the loan file.

   ii. If the Environmental Professional conducting the Transaction Screen concludes that further investigation is warranted, the SBA Lender must obtain a Phase I ESA. If an Environmental Professional recommends proceeding directly from the Transaction Screen to a Phase II (thus bypassing the Phase I), and the SBA Lender concurs, the SBA Lender must seek in advance an exception to policy from the SBA Environmental Committee, which may be granted on a case-by-case basis.

e. Phase I ESA Results:

   i. If the Environmental Professional conducting the Phase I ESA concludes that no further investigation is warranted, the SBA Lender must keep a copy of the Phase I ESA and review in the loan file.

   If the Environmental Professional conducting the Phase I ESA concludes that further investigation is warranted (typically a Phase II), and the SBA Lender still wants to make the loan, the SBA Lender must proceed as recommended by the Environmental Professional, or in the alternative submit results for an exception to policy at EnvironmentalAppeals@sba.gov. In requesting an exception to policy, the SBA Lender must provide the SBA Environmental Committee with justification for the exception at EnvironmentalAppeals@sba.gov. SBA will require compliance with all of an Environmental Professional's recommendations (including "housekeeping

measures," such as secondary containment, decommissioning monitoring wells, sealing floor drains, etc.).

ii. In the rare instance where an exception to policy may be warranted, SBA Lenders must provide the SBA Environmental Committee with justification for not wanting to follow the Environmental Professional's recommendations and obtain committee approval.

f. Phase II ESA Results:

i. If the Environmental Professional conducting the Phase II ESA concludes that no further investigation is warranted, the SBA Lender must retain a copy of the environmental documents and review in the loan file.

ii. If the Phase II ESA reveals Contamination and the SBA Lender still wishes to make the loan, the SBA Lender must ensure that the Environmental Professional has documented:

a) Whether the Contamination quantities exceed the reportable or actionable levels;

b) Whether Remediation is necessary;

c) An estimate of any Remediation costs (Environmental Professionals may use ASTM E2137-22 Standard Guide for Estimating Monetary Costs and Liabilities for Environmental Matters); and

d) The projected completion date of any Remediation.

iii. If the Environmental Investigation reveals Contamination, the SBA Lender should determine whether disbursement is appropriate under one or more of the factors identified below in Paragraph 5, Property Contamination or Remediation.

5. Property Contamination or Remediation

Loans may not be approved or disbursed if there is known Contamination or on-going Remediation at the Property unless the risks have been minimized to the satisfaction of SBA. SBA Lenders seeking loan approval or disbursement authority despite Contamination or on-going Remediation at the Property must submit a recommendation to SBA that includes, at a minimum, a discussion of the following:

a. Nature and Extent of the Contamination including copies of the following documents pertaining to the Property:

i. All relevant Environmental Investigation Reports;

ii. All publicly available Governmental Entity correspondence.

b. Remediation:

i. Recommended method of Remediation;

ii. Status of on-going Remediation, if any;

iii. Environmental Professional's estimated cost of Remediation;

iv. Environmental Professional's estimated completion date;

v. Governmental Entity's designation of responsible Person(s) (as defined in 13 CFR § 120.10);

vi. Person(s) paying for on-going Remediation;

c. Collateral Value:

i. Proposed loan amount and proposed use of proceeds;

ii. Appraised or the estimated value of the Property;

iii. Institutional Controls and Engineering Controls, if any, and their impact on repayment ability, collateral value, and marketability of the Property; and

d. Mitigating Factors:

SBA will rely upon one or more of the following factors when deciding to disburse before completion of Remediation or monitoring.

i. Indemnification. If any Person (as defined in Appendix 4) who possesses sufficient financial resources to cover the costs of completing Remediation executes the SBA Environmental Indemnification Agreement in Appendix 8, approval or disbursement may be considered. The SBA Lender must conduct an analysis of the proposed indemnitor to ensure that it has sufficient assets to honor an indemnification agreement. The Third Party Indemnitor cannot be the Applicant or the operating company.

The SBA Environmental Indemnification Agreement:

a) Cannot be modified;

b) Must be executed by the Applicant and (if applicable) Operating Company;

c) Must have a copy of the Environmental Investigation Report attached to it; and

d) Must be properly recorded in the memorandum format in Exhibit C to Appendix 8.

For 7(a) loans: All 7(a) Lenders (except when submitting requests through PLP, 7(a) Small Loans, SBA Express and Export Express) must submit the finalized SBA Environmental Indemnification Agreement to SBA for review and approval prior to a request that SBA fund the loan.

For 504 loans: All CDCs, including PCLP CDCs, must submit each finalized SBA Environmental Indemnification Agreement (located in Appendix 8 of this SOP) to the SLPC for review and approval no less than 2 weeks in advance of submission of the loan closing package if they want the loan to be considered in that closing cycle.

ii. Completed Remediation. If the Governmental Entity has affirmed in writing that active Remediation is complete but additional monitoring is required, approval or disbursement may be considered after the following occurs:

a) Monitoring results for the first year are obtained;

b) An Environmental Professional concludes that the results show no unacceptable increase in Contamination since Remediation; and

c) An Environmental Professional concludes that the owner/operator of the Property is in compliance with any continuing obligations, including activity and use limitations, Engineering and Institutional Controls, and post-Remedial monitoring required by the Governmental Entity.

iii. No Further Action. If an SBA Lender obtains a "no further action letter" or "closure letter" from a Governmental Entity (or state equivalent of a "no further action letter" or "closure letter") stating that no further Remediation or monitoring of Contamination previously found is required, approval or disbursement may be considered. A state equivalent of a closure letter includes a written determination from a licensed professional in those jurisdictions that delegate authority to such professionals for site closures.

iv. Minimal Contamination with Minimal Remediation. If the extent of Contamination and cost of Remediation are de minimis in relation to the value of the Property and/or the resources of the Person responsible for Remediation, and the Remediation is projected to be completed within 1 year, approval or disbursement may be considered. The SBA Lender should identify the Environmental Professional that will supervise the Remediation and discuss:

a) The nature of the Contamination;

b) The reliability of the Remediation estimates;

c) The projected completion date; and

d) The duration of ongoing monitoring.

v. Clean-up Funds. If the SBA Lender provides evidence from a Governmental Entity that the Applicant or Property has been approved by a fund to pay for or reimburse Remediation costs, and the amount allocated is sufficient to cover the costs of Remediation, approval or disbursement may be considered.

The SBA Lender must also address any conditions of Remediation that might preclude payment or reimbursement and the financial capability of the fund.

vi. Escrow Account. If an escrow account is available that equals a minimum of 150 percent of the total estimated cost of required Remediation and is controlled by a 7(a) Lender or first mortgage holder in a 504 loan as trustee, approval or disbursement may be considered. The Governmental Entity must concur with the Remediation's scope. The escrow agreement for the escrow account must ensure that escrow funds will only be used for Remediation costs. The source of the escrow funds may not be SBA Loan proceeds. Depending upon the circumstances, an escrow account with more than 150 percent of the estimated costs of Remediation may be appropriate. The escrowed funds may be used for Remediation. Any remaining funds in the account may not be released until the appropriate "closure letter" or "no further action letter" is received or, in the case of monitoring, when all monitoring wells related to the Property have been decommissioned.

Note: The SBA Lender's, or for 504 loans, the Third Party Lender's role as trustee of the escrow account is solely to release funds upon the satisfactory completion of Remediation work – the SBA Lender or Third Party Lender must not control or manage the Property being remediated.

vii. Contamination Originating from another Site. If Contamination on the Property is shown to have come from another property, approval or disbursement may be considered if:

a) Another Person with sufficient resources is performing Remediation pursuant to a Remediation action plan that has been approved by the appropriate Governmental Entity; or

b) The state has laws or regulations that provide that an owner or operator of property will not be responsible for Contamination from another site; or

c) The Governmental Entity provides satisfactory written assurance that it will not hold the Property owner liable for the Contamination. The SBA Lender should attempt to have the SBA Lender and SBA included by name in the letter along with the Property owner and future purchasers.

viii. Additional or Substitute Collateral. If additional or substitute collateral is being pledged, or an additional equity contribution is being made, sufficient to overcome the potential loss due to Contamination, then approval or disbursement may be considered.

ix. Other Factor(s). The SBA Lender and SBA may rely on factors other than or in addition to the eight referenced above when considering approval or disbursement. For example, the existence of adequate environmental

insurance that is already in place and already paying remediation costs, bonds, agreements not to sue present and future property owners from the Governmental Entity, brownfields agreements, Engineering and Institutional Controls, etc. However, reliance solely upon "Other Factor(s)" requires clearance from the SBA Environmental Committee. This requirement extends to loans processed under delegated and non-delegated procedures. **Lenders seeking to rely solely on "Other Factor(s)", regardless of whether processing a loan under delegated or non-delegated procedures**, **must forward the Environmental Investigation Report(s) with a memorandum setting forth their request to EnvironmentalAppeals@sba.gov.** (NOTE: This email address cannot receive submissions larger than 15MB. If the email and attachments exceed this size, the request must be sent in more than one email.)

e. For 7(a) loans processed under delegated authority, including 7(a) Small Loans, SBA Express and Export Express, 7(a) Lenders must follow these guidelines, but they do not have to submit documentation or obtain SBA's concurrence prior to approval or disbursement of the loan, unless they are relying solely upon Paragraph d. ix, Other Factor(s) immediately above.

6. Special Use Facilities

a. Child-Occupied Facilities

Prudent lending practices dictate that specific additional environmental assessments be performed for Child-Occupied Facilities (see definition in Appendix 4). Such facilities, constructed prior to 1978, must undergo a lead risk assessment and also testing for lead in drinking water at all taps and fountains potentially used as a drinking water source for children. A new lead risk assessment and new testing for lead in drinking water at all indoor and outdoor taps and fountains accessible to children and, therefore, potentially used as a drinking water source for children are required for each new loan. The assessment and any tests must have been conducted within one year of the date of issuance of the SBA loan number. All lead assessments must be conducted in conformance with U.S. Environmental Protection Agency (EPA) regulations at 40 CFR Part 745 and U.S. Department of Housing and Urban Development (HUD) Guidelines for the Evaluation and Control of Lead-Based Paint Hazards in Housing Second Edition, July 2012. The results of these assessments must be ***retained in the loan file***. The SBA Lender may not disburse the loan unless the risk of lead exposure to infants and small children has been sufficiently minimized.

b. Drycleaners

On-site dry cleaning facilities, which may have utilized chlorinated solvents such as tetrachloroethene (PCE) and trichloroethene (TCE) and/or petroleum-based

solvents in the course of their business operations, may present significant clean-up costs if these contaminants have entered the soil, soil vapor and/or groundwater. Prudent lending practices dictate and SBA requires that for any Property with on-site dry cleaning facilities, whether currently in operation or operated historically at the site, that uses, used, or likely used chlorinated and/or petroleum-based solvents, a Phase I followed by a Phase II Environmental Assessment is required. (Any deviation from this requirement must be directed to EnvironmentalAppeals@sba.gov as a request for an exception to policy). For on-site dry cleaners, the investigation must address soil, groundwater, and soil vapor. A Phase II performed in connection with an on-site dry cleaning facility must be conducted by an independent Environmental Professional *who holds a current Professional Engineer's or Professional Geologist's license and has the equivalent of 3 years of full time relevant experience.*

c. Gasoline Stations

Gasoline stations also present significant clean-up costs if contaminated (for specific requirements pertaining to gasoline stations, please refer to Appendix 7).

7. Release of Rights to Indemnification from SBA/Lender

If any Person has a right to indemnification from subsequent owners of the Property (e.g., SBA or SBA Lender after acquiring Property through foreclosure or other means), then they must execute either the SBA Indemnification Agreement or another document in which they waive all known and unknown rights and release all claims and causes of action whether now or hereafter in existence against SBA and the SBA Lender related to Contamination at the Property including the right to indemnification. The document containing the waiver and release must be recorded.

Additionally, for 504 loans: SBA Lenders must submit all waiver and release documents to the SBA via the SBA Loan System for review and approval by local SBA counsel, along with a copy of the title report, the document providing for indemnification, and the purchase and sale documents, if any. PCLP CDCs must also submit the waiver and release to the SBA via the SBA Loan System for review and approval prior to a request that SBA fund the loan.

8. Brownfields Sites

SBA encourages the redevelopment of brownfields, and SBA Loan guarantees are available to small businesses interested in locating on revitalized brownfields. Typically, this occurs through utilization of one or more of the nine Mitigating Factors in Paragraph 5.d. above.

9. Questions on SBA's Environmental Policy and Appeals

Questions on SBA's Environmental Policy should be directed to local SBA counsel for the area where the Property is located.

SBA Lenders who believe that an environmental decision that has been rendered by SBA is inconsistent with this SOP may appeal the decision by forwarding a copy of the decision, along with an explanation of how the determination is perceived to be inconsistent with this SOP to EnvironmentalAppeals@sba.gov.

(NOTE: This email address cannot receive submissions larger than 15MB. If the email and attachments exceed this size, the appeal must be sent in more than one email.)

Environmental appeals, including exceptions to Agency environmental policy, will be reviewed by the SBA Environmental Committee comprised of OGC attorneys appointed by the Associate General Counsel for Litigation, who may consult with an environmental engineer. The Associate General Counsel for Litigation retains the authority to overrule decisions rendered by the SBA Environmental Committee.

## SECTION B. 7(A) LOAN PROGRAM SPECIFIC REQUIREMENTS

This section, along with Section A, Core Requirements for all 7(a) and 504 Loans, contains the policies and procedures governing SBA's 7(a) business loan programs. Because Paycheck Protection Program (PPP) loans authorized under § 7(a)(36) of the Small Business Act are 7(a) loans, this SOP applies to the making of PPP loans, to the extent that the SOP is not superseded by or in conflict with PPP-specific requirements. **Lenders must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.**

SBA recognizes the importance of giving special consideration to veterans in its loan programs. SBA will prioritize processing applications from businesses that are owned by veterans when those loans are processed by SBA under non-delegated procedures. For loans processed under delegated procedures, SBA encourages Lenders to give special consideration to veterans during application processing.

# CHAPTER 1: STANDARD 7(A) LOANS (LOANS GREATER THAN $350,000)

This Chapter covers Standard 7(a) Loans, which are 7(a) loans that are greater than $350,000, and exclude 7(a) Small, SBA Express, Export Express, CAPLines, Export Working Capital Program (EWCP), International Trade loans, and Pilot Program loans.

**Lenders must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.**

## A. ELIGIBLE USES OF PROCEEDS

In addition to the eligible uses of proceeds in the Core requirements, Standard 7(a) Loans may use loan proceeds for:

1. Debt Refinancing: See Appendix 14: Debt Refinancing Para. B.1, for all debt refinancing requirements for Standard 7(a) loans.
2. Change of Ownership: See Appendix 15: 7(a) Changes of Ownership

## B. LOAN TERMS AND CONDITIONS

1. Maximum Loan Amount
    a. The maximum loan amount for any one Standard 7(a) loan is $5,000,000.
    b. Maximum Loans to Businesses with Affiliates

    13 CFR § 120.151 Lenders must determine whether the Applicant has any affiliates and document the results in their credit analysis. If affiliation exists, SBA's loan maximums apply to the Applicant, including all affiliates, as if all were a single business.
2. Maximum Guaranty Amounts and Percentages: See Appendix 16: 7(a) Maximum Guaranty Amounts and Percentages Para. B.1.
3. Loan Maturities: See Appendix 17: 7(a) Loan Maturity Requirements Para. B.1.
4. Interest Rates: See Appendix 18: 7(a) Interest Rate Requirements Para. B.1.

    SBA QUICK REFERENCE CHART: Maximum Interest Rates Allowed

| Product<br>Standard 7(a) Loans | Interest Rate<br>The maximum allowable fixed rate is available on SBA's Wiki page. Maximum variable rates are: |
|---|---|
| Loans $50,000 or less | Cannot exceed Prime or SBA Optional Peg Rate + 6.5% |
| Loans $50,001 up to and including $250,000 | Cannot exceed Prime or SBA Optional Peg Rate + 6.0% |

| Product<br>Standard 7(a) Loans | Interest Rate<br>The maximum allowable fixed rate is available on SBA's Wiki page. Maximum variable rates are: |
|---|---|
| Loans $250,001 up to and including $350,000 | Cannot exceed Prime or SBA Optional Peg Rate + 4.5% |
| Loans $350,001 and greater | Cannot exceed Prime or SBA Optional Peg Rate + 3.0% |

## C. CREDIT STANDARDS

The policies that make up SBA's credit standards begin with the requirements outlined in 13 CFR §§ 120.101 and 120.150. This section provides procedural guidance as to what the Lender should or must consider when analyzing any request for financial assistance that will be guaranteed by SBA.

A Lender must analyze each application in a commercially reasonable manner, consistent with prudent lending standards. The cash flow of the Applicant is the primary source of repayment, not any expected recovery from the liquidation of collateral. Thus, if the Lender's financial analysis demonstrates that the Applicant lacks reasonable assurance of repayment in a timely manner from the cash flow of the business, the loan request must be declined, regardless of the collateral available or outside sources of repayment.

1. Processing Methods

    a. Non-delegated – When a Lender submits a Standard 7(a) loan guaranty request under the non-delegated processing method, the Lender submits the application and supporting documents to SBA. SBA will make the final determination as to the eligibility and creditworthiness of the Applicant, including approving the uses of proceeds, the adequacy of the collateral being pledged, the structure of the loan, and any equity contribution to be required from the Applicant.

    b. PLP – When a Lender submits a Standard 7(a) loan guaranty request under the Lender's PLP authority, the Agency does not review the Lender's analysis of the credit or structure of the loan or line of credit prior to issuing a loan number. The Lender must analyze creditworthiness in accordance with SBA Loan Program Requirements and properly document its file. The PLP Lender's analysis is subject to SBA's review and determination of adequacy when the Lender requests SBA to purchase its guaranty or when SBA is conducting lender oversight activities.

2. Underwriting Standard 7(a) Loans:

    a. Lender's Credit Analysis:

    The Lender's credit memorandum and analysis must address the Applicant's ability and likelihood to repay the loan from the cash flow of the business and past performance by documenting the following:

i. A description and history of the business, including:

a) Nature of the business;

b) Length of time in business under current management;

c) Depth of management experience in the industry or a related industry;

d) Brief description of the business's management team including principal's involvement in the daily onsite management of the business or how the daily operations will be managed if the principals are not there on a daily basis.

e) If the daily operations will be handled under a management agreement, Lenders must obtain a copy of the management agreement (unless the management agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory), review it to determine if it results in an ineligible passive business, and retain in their loan file.

ii. Financial analysis of repayment ability:

a) For existing businesses based on the three most recent years of historical financial information (tax returns or balance sheet with debt schedule and income statement) plus an interim financial statement. (13 CFR § 120.191)

b) For start-ups, new businesses, changes of ownership, and other applications based on projections, include detailed projections, including the supporting assumptions that reflect a debt service coverage equal to or greater than 1.15 within 2 years from loan funding or, for construction projects, within 2 years from the end of construction.

c) Review and analyze the Applicant(s), Associate(s), and Guarantor(s) credit reports and discuss any credit issues.

i) For loans processed under non-delegated authority, Lenders should include a copy of the credit report, dated within 90 days, with the documents submitted in the SBA Loan System.

d) The financial analysis for all Applicants must address the following as applicable:

i) Historical cash flow for existing businesses, that demonstrates total debt service coverage after the SBA loan; if the historical cash flow from the most recent full year and the interim financial statements do not show sufficient debt service coverage, Lender must obtain from the Applicant and analyze 2 years of detailed projections including the supporting assumptions justifying relying on projections instead of

historical performance;

ii) Calculation of earnings before interest, taxes, depreciation, and amortization (EBITDA);

iii) Justification for additions and subtractions to cash flow such as the following:

(a) Unfunded capital expenditures;

(b) Non-recurring income;

(c) Expenses and distributions;

(d) Distributions for S-Corp taxes;

(e) Rent payments;

(f) Owner's Draw; and/or

(g) Global cash flow analysis that includes assessment of impact on cash flow to/from any affiliate business. Anticipated cash flow from rental income from the Project Property may be included in the global cash flow analysis;

iv) The effect any affiliates may have on the ultimate repayment ability of the Applicant.

iii. Debt Service (DS) is defined as the future required principal and interest payments on all business debt inclusive of new SBA loan proceeds. The Applicant's debt service coverage ratio (DSC) must be equal to or greater than 1.15 on a historical and/or projected cash flow basis and 1:1 on a global basis. To perform a complete analysis of debt service coverage, it is important for a Lender to obtain a current debt schedule prepared by the Applicant, including any shareholder debt.

iv. For cash flow projections, the Lender must calculate the debt service coverage (which may not include anticipated cash flow from rental income from the Project Property) and provide the assumptions supporting the projected cash flow coverage, including as applicable:

a) Justification for revenue growth, i.e., new product lines, sales channels, and new production facilities;

b) Justification for any reduction in expenses; and

c) A comparison to current industry trends.

v. Spread of pro-forma Business Balance Sheet (current business balance sheet adjusted for all changes in assets and liabilities as a result of the SBA loan, other debt, any required equity injection and use of loan proceeds);

vi. Ratio calculations (based on the pro-forma Balance Sheet and historical and projected Income Statements) for the following financial ratio benchmarks: Current Ratio, Debt/Tangible Net Worth, Debt Service Coverage, and any other ratios the Lender considers significant for the business/ industry (e.g., inventory turnover, receivables turnover, and payables turnover, etc.) including discussion of Lender's comparison to industry trends;

vii. Analysis of working capital adequacy, at a minimum over the next 12 months;

viii. Assessment of collateral adequacy adjusted in accordance with Appendix 19 to offset risk of default;

ix. Insurance Requirements, including:

a) Life Insurance – on whom and how much. If life insurance will not be required, provide justification.

b) Business hazard & liability insurances.

x. Explanation of and justification for the refinancing of any debts as part of the loan request, along with supporting documentation, in accordance with the debt refinancing requirements in Appendix 14: 7(a) Debt Refinancing Requirements, including a written explanation for any late payments over the past 12 months.

xi. Lender's rationale for recommending approval, including a discussion and analysis of the following:

a) The factors demonstrating the Applicant does not have credit available elsewhere on reasonable commercial terms from non-Federal, non-State, non-local government sources in accordance with Section A, Ch. 1. Para. H.

b) When 50 percent or more of the loan proceeds will be used for working capital, Lender must explain in its credit memorandum why this level of working capital is necessary and appropriate for the subject business;

c) Competition;

d) Seller financing;

e) Stand-by agreements;

f) 90+ day delinquencies;

g) Trade disputes and/or;

h) Federal, State, or local citations which would preclude the Applicant from normal business operations;

i) For a change of ownership, discussion/analysis of the business valuation used to support the purchase price (see Appendix 15 Para. C.1.a, Business Valuation Requirements - change of ownership);

j) Discussion of any liens, judgments, bankruptcy filings or pending litigation including divorce proceedings;

k) If the application involves a franchise (as defined by FTC), the Lender must review any credit information provided, such as the number of failed franchisees and cash flow projections provided by the franchisor).

l) Discussion of other relevant information.

b. Equity requirements (13 CFR § 120.150):

i. Depending on whether the loan is processed on a non-delegated or PLP basis, the Lender or SBA must determine that there is sufficient invested equity. To do this, the Lender (for PLP loans) or SBA (for non-delegated loans) must determine if the equity position, any required equity contribution, and the pro forma debt-to-worth are acceptable based on the factors related to the type of business, experience of management, and the level of competition in the market area. The Lender must include in its credit memorandum a detailed discussion of the equity position (net worth) and any required equity injection. See Ch. 6, Para. D.3., Closing Documentation, for requirements concerning documenting and verifying equity injection.

ii. Minimum equity injection requirements for Start-Up Businesses: SBA considers a business to be a "start-up" for the purpose of determining equity injection requirements if it has been in operation (i.e., generating revenue from intended operations) for 1 year or less. SBA considers an equity injection (Applicant contribution) of at least 10 percent of the total project costs (all costs required to become operational, regardless of the source of funds, except for lines of credit and 504 loans) to be necessary for a Start-Up Business to operate on a sound financial basis. All 7(a) loans made to a Start-Up Business require a 10% equity injection based on the project cost; however, loans approved more than 90 days apart from each other are considered to be separate projects.

iii. Changes of ownership: See Appendix 15: 7(a) Changes of Ownership for specific change of ownership equity requirements.

iv. Source of Equity Injection: The following may be considered equity injection.

a) Standby Agreements - only debt that is on full standby (no payments of principal or interest for the term of the 7(a) loan) may be considered as equity for SBA's purposes. Lender must use SBA Form 155 or its own

equivalent Standby Agreement form, and a copy of the note must be attached to the standby agreement. The standby debt may accrue interest and may be added to the standby debt and amortized after the 7(a) loan is paid in full. Standby Creditor must subordinate any lien rights in collateral securing the loan to Lender's rights in the collateral and take no action against Borrower or any collateral securing the Standby Debt without Lender's consent.

b) Cash that is not borrowed, whether on the business's balance sheet or from other sources.

c) Cash that comes from a personal loan where repayment can be demonstrated to come from a source other than the cash flow of the business (the salary paid to the owner by the business does not qualify).

d) Grants that do not have repayment or clawback provisions during the life of the 7(a) loan.

e) Assets other than cash – An appraisal or other valuation by an independent third party is required if the valuation of the fixed assets is greater than the Net Book Value. A valuation of the fixed assets provided as part of a business valuation will not meet these requirements.

f) Eligible prepaid expenses that the Lender has verified by obtaining paid invoices, canceled checks, or bank statements. Lender must retain copies of the documentation in the loan file.

i) Expenses related to education, advisory services, or fees paid by the Applicant to an Agent are not eligible prepaid expenses and are not considered equity.

g) An equity investment not subject to an agreement to repay equity or make distributions to recover an investor's investment prior to release of the guaranty. Note: SBA considers any investment subject to an agreement to repay equity or make distributions to recover an investor's investment prior to release of the guaranty (e.g., certain types of redeemable preferred stock) to be debt and not equity.

3. Collateral

See Appendix 19: 7(a) Collateral Requirements and paragraph B. Program-Specific Requirements.

See Section A, Ch. 5, Para. A. for guaranty requirements.

## D. SUBMISSION OF APPLICATION FOR GUARANTY

See Appendix 20: Submission of Application for Guaranty

## CHAPTER 2: 7(A) SMALL & SBA EXPRESS

**7(a) Small loans** are term (non-revolving) 7(a) loans that are $350,000 or less. 7(a) Small loans exclude: Standard 7(a) loans, SBA Express, Export Express, CAPLines, Export Working Capital Program (EWCP), and Pilot Program loans.

**SBA Express** loans are loans that are $500,000 or less and may only be made by a Lender with SBA Express authority. SBA Express Lenders may ***not*** request that an SBA Express loan be processed under non-delegated authority by SBA's LGPC.

SBA Express was established as a permanent SBA program under P.L.108-447 and signed into law on December 8, 2004. The program reduces the number of government mandated forms and procedures, streamlines the processing, and reduces the cost of smaller, less complex SBA loans. The program allows Lenders to use, to the maximum extent practicable, their respective loan analyses, procedures, and documentation.

### Lenders must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.

### A. ELIGIBLE USES OF PROCEEDS

Lenders must apply and comply with all of SBA's Loan Program Requirements, including the Core Requirements in Section A of this SOP.

Loan proceeds must be used exclusively for business-related purposes, subject to 13 CFR §§ 120.120 and 120.130

In addition to the Core Requirements for all 7(a) and 504 Loans identified in Section A of this SOP, loan proceeds may be used for:

1. Debt Refinancing: See Appendix 14: 7(a) Debt Refinancing Requirements Para. B.2.
2. Changes of Ownership: See Appendix 15: 7(a) Changes of Ownership

   Change of Ownership transactions cannot be financed using 7(a) Small standards and must be underwritten per the requirements outlined in Appendix 15.

### B. LOAN TERMS AND CONDITIONS

Lenders must comply with the requirements in Section A, Ch. 4, Para. C, 7(a) Loan Program Fees, and Section A, Ch. 4, Para. D., 7(a) Loan Program and Use of Agents.

1. Maximum Loan Amount
   a. 7(a) Small loans have a maximum loan amount of $350,000 per project (including other 7(a) loans made within 90 days).
   b. The maximum aggregate SBA Express loan amount is $500,000 (gross), inclusive of all outstanding SBA Express, Community Advantage Pilot loans, Community Express, and Patriot Express loans the Applicant and its Affiliates may have. For

Community Advantage Small Business Lending Companies (CA SBLCs), the maximum loan amount to any one Borrower is limited to $350,000.7(a) Small loans are not included in this limit.

c. Maximum Loans to Businesses with Affiliates.

13 CFR § 120.151 Lenders must determine whether the Applicant has any affiliates and document the results in their credit analysis. If affiliation exists, SBA's loan maximums apply to the Applicant, including all Affiliates, as if all were a single business.

2. Maximum Guaranty Amounts and Percentages: See Appendix 16: 7(a) Maximum guaranty Amounts and Percentages Para.B.2.

3. Loan Maturities: See Appendix 17: 7(a) Loan Maturity Requirements Para. B.2-3.

   a. SBA Express lines of credit: See Appendix 19 Para. B.3.

   b. Lenders have the ability to reissue a new SBA Express loan to restructure a current SBA Express loan at any point before amortizing payments begin.

      i. Option #1 - Line Retention: When reissuing a new SBA Express loan to retain the revolving period, the Lender must address the overall line utilization in their credit memo and justify why the line needs to be retained.

      ii. Option #2 - Extended Amortization: Lenders may reissue a new SBA Express to term out their existing SBA Express loan with a term that does not exceed 10 years. This option expressly allows a Lender to establish a longer amortization term that exceeds an initial repayment term of the initial SBA Express loan. When utilizing this option, the new Express loan may not have a revolving period.

4. SBA Express Non-Financial Default Provisions:

   Non-financial default provisions are allowed under SBA Express under the following conditions:

   a. Non-financial default provisions are loan conditions that, if violated, would cause the loan to be in default even though the Borrower has made all payments as agreed.

   b. Non-financial default provisions must be substantive and must be agreed to by the Borrower in writing at loan closing;

   c. The provisions must be consistent with those used by the Lender on its similarly-sized non-SBA guaranteed commercial loans;

   d. A lender may not request purchase of the guaranty solely based on a violation of a non-financial default provision (see 13 CFR § 120.520); and

   **e.** A maturity date must be established in the note. For example, a line of credit

could state that it is payable upon demand under certain conditions, but in no case later than a certain date.

5. Interest Rates: See Appendix 18: 7(a) Interest Rate Requirements Para. B.2-3.

SBA QUICK REFERENCE CHART: Maximum Interest Rates Allowed (See additional information below)

| **Product**<br>**7(a) Small and SBA Express Loans** | **Interest Rate**<br>**The maximum allowable fixed rate is available on SBA's Wiki page. Maximum variable rates are:** |
|---|---|
| Loans $50,000 or less | Cannot exceed Prime or SBA Optional Peg Rate + 6.5% |
| Loans $50,001 up to and including $250,000 | Cannot exceed Prime or SBA Optional Peg Rate + 6.0% |
| Loans $250,001 up to and including $350,000 | Cannot exceed Prime or SBA Optional Peg Rate + 4.5% |
| SBA Express Loans $350,001 up to and including $500,000 | Cannot exceed Prime or SBA Optional Peg Rate + 3.0% |

## C. CREDIT STANDARDS FOR 7(A) SMALL LOANS & SBA EXPRESS

The policies that make up SBA's credit standards begin with the requirements outlined in 13 CFR §§ 120.101 and 120.150. This section provides procedural guidance as to what the Lender should or must consider when analyzing any request for financial assistance that will be guaranteed by SBA.

A Lender must analyze each application in a commercially reasonable manner, consistent with prudent lending standards. The cash flow of the Applicant is the primary source of repayment, not any expected recovery from the liquidation of collateral. Thus, if the Lender's financial analysis demonstrates that the Applicant lacks reasonable assurance of repayment in a timely manner from the cash flow of the business, the loan request must be declined, regardless of the collateral available or outside sources of repayment.

To the maximum extent practicable, 7(a) Small and SBA Express Lenders may use their own forms, internal credit memoranda, notes, collateral documents, and servicing and liquidation documentation. In using their documents and procedures, Lenders must follow their established and proven internal procedures used for their similarly-sized, non-SBA guaranteed commercial loans.

1. Processing Method

    a. 7(a) Small loans:

        i. Non-delegated – When a Lender submits a loan guaranty request under the non-delegated processing method, the Lender submits the application and supporting documents to SBA.

ii. PLP – When a Lender submits a loan guaranty request under the Lender's PLP authority, the Agency does not review the Lender's analysis of the credit or structure of the loan or line of credit prior to issuing a loan number. The Lender must analyze credit worthiness in accordance with SBA Loan Program Requirements and properly document its file. The PLP Lender's analysis is subject to SBA's review and determination of adequacy when the Lender requests SBA to purchase its guaranty or when SBA is conducting lender oversight activities.

**b.** SBA Express loans are ***only*** processed via an SBA Express Lender's delegated authority. When a Lender submits an SBA Express loan guaranty request under the Lender's SBA Express authority, the Agency does not review the Lender's analysis of the credit or structure of the loan or line of credit prior to issuing an SBA Loan Number. The Lender must analyze credit worthiness in accordance with SBA Loan Program Requirements and properly document its file. The SBA Express Lender's analysis is subject to SBA's review and determination of adequacy when the Lender requests SBA to purchase its guaranty or when SBA is conducting lender oversight activities.

2. Underwriting

Note: 7(a) Small Loans may only be increased up to $350,000. If the 7(a) Small loan is increased above $350,000, it becomes a Standard 7(a) loan and must follow the requirements in Chapter 1 of this section. SBA Express loans may not exceed $500,000.

**a. Underwriting 7(a) Small Loans**

i. Lenders must use appropriate, prudent, and generally accepted industry credit analysis processes and procedures consistent with those used for the Lender's similarly-sized, non-SBA guaranteed commercial loans to determine the Applicant's Credit History and Repayment Ability. These policies and procedures may include credit scoring models that are permitted by the Lender's primary Federal regulator for the purpose of analyzing the credit history of the Applicant.

ii. In addition to summarizing the operating business, ownership, and loan request, the Lender's credit memorandum must state why credit is not available elsewhere, and include the following:

a) "Credit History": Analysis of the credit history of the Applicant (and Operating Company, if applicable), its Associates, and guarantors;

i) Review and analyze the Applicant(s), Associate(s), and Guarantor(s) credit reports and discuss any credit issues.

(a) For loans processed under non-delegated authority, Lenders should include a copy of the credit report, dated within 90 days, with the

documents submitted in E Tran.

ii) The Lender may use a scoring model that combines the Applicant and guarantors as long as its use is permitted by its primary Federal regulator, it is used for its similarly-sized, non-SBA guaranteed loans, and the model does not rely solely on consumer credit scores.

iii) The results of the credit history analysis must be documented in the credit memorandum. If a scoring model is used, the results (e.g., score) must be stated in the credit memorandum along with the acceptable approval range.

iv) An SBLC may use credit scoring. If it does, SBA may request that the SBLC periodically provide the credit scoring model to SBA for review.

b) "Repayment Ability": Analysis of the Applicant's (and Operating Company, if applicable) debt service coverage, and projected earnings and assumptions (if applicable);

i) The two most recent months of commercial bank activity or statements, from the time of application, for the primary operating account must be reviewed as part of the Analysis to determine whether all debts were included in the debt service coverage calculation, and statements must be retained in the loan file.

ii) For 7(a) Small Loans, the Applicant's debt service coverage ratio must be equal to or greater than 1.10:1 on either a historical or projected basis.

(a) Debt service coverage is measured by dividing the operating cash flow (OCF) by the debt service (DS). The Lender must obtain, analyze, and retain in their files the financial statements and projections necessary to calculate the required debt service coverage ratio.

(i) Operating cash flow (OCF) is defined as earnings before interest, taxes, depreciation, and amortization (EBITDA). Lenders may make additions and subtractions to OCF pursuant to the rules found in Section B, Ch. 1, Para. C.2.a.ii.c), Credit Standards (Page 131).

(ii) Debt service (DS) is defined as the future required principal and interest payments on all business debt, inclusive of new SBA loan proceeds.

(b) The debt service coverage ratio must be calculated using one of the following:

(i) Last year-end financial statement (tax return, internal statement, or accountant-prepared), which must be dated and received within 120 days of year end.

(ii) Last year-end statement plus interim financial statement. Lenders will calculate the debt service coverage ratio using the last year-end statement while also confirming that there has not been a decline in the financial condition of the Applicant during the interim period. Interim financial statements must be dated within 120 days of submission to SBA.

(iii) 12-month projections, including supporting assumptions. When using projections, the Applicant must demonstrate a debt service coverage equal to or greater than 1.10:1 within one year of loan funding. This method is not applicable to change of ownership transactions, and the change of ownership rules for DSC must be adhered to as outlined in Appendix 15 – 7(a) Changes of Ownership.

iii) Lenders must obtain and analyze the two most recent months of commercial bank activity or statements on the primary operating account and include them within their credit file. The commercial bank activity is to be used by the Lenders to confirm the commercial debts and obligations in the debt service coverage calculation.

(a) If the Lender is underwriting an Applicant that is not currently in operation and has no commercial debts or obligations, they are not required to obtain two months of commercial bank activity or statements on the primary operating account.

(b) If the Lender is underwriting an Initial Acquisition change of ownership transaction and there are no other debts or obligations beyond the 7(a) loan, they are not required to obtain two months of commercial bank activity or statements on the primary operating account.

iv) If the Lender has calculated an acceptable debt service coverage ratio and reviewed two months of commercial bank activity to confirm the commercial debts and obligations, the requirement to determine the Repayment Ability is satisfied.

v) If the Applicant does not meet or exceed the required debt service coverage ratio, the loan must be processed following the procedures for either Standard 7(a) or SBA Express Loans.

c) Insurance – Lender must address whether life insurance or other insurance (i.e., insurance other than hazard insurance) will be required.

For insurance other than hazard insurance, Lender may follow the same written policies and procedures it uses for its similarly-sized, non-SBA guaranteed commercial loans. Hazard insurance is required in accordance with Section A, Ch. 5, Para. C.1.

d) Lender must address other specifics relating to the loan as applicable, including:

i) A description of any proposed collateral and estimated value;

ii) For loans greater than $50,000, when 50 percent or more of the loan proceeds will be used for working capital, Lender must explain in its credit memorandum why this level of working capital is necessary and appropriate for the subject business;

iii) The terms of any seller financing and standby agreements;

iv) Discussion of any liens, judgments, or pending litigation, including divorce proceedings;

v) If the application involves a franchise (as defined by FTC), the Lender must review any credit information provided, such as the number of failed franchisees and cash flow projections provided by the franchisor. Lender must review any management agreement (unless the management agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory) to determine if it results in an ineligible passive company;

vi) Any debt refinancing, including justification and original purpose (copies of all notes to be refinanced must be submitted with any loan submitted to the LGPC).

vii) The effect any affiliates may have on the ultimate repayment ability of the Applicant.

iii. 7(a) Small Equity Requirements.

a) The Lender must include in its credit analysis a detailed discussion of the required equity and its adequacy. See Ch. 6, Para. D.3.f. of this section for requirements concerning documenting and verifying equity injection.

b) Minimum equity injection requirements for certain Applicants and loans:

i) Start-Up Businesses – SBA considers a business to be a “start-up” for the purpose of determining equity injection requirements if it has been in operation (i.e., generating revenue from intended operations) for 1 year or less. SBA considers an equity injection (Applicant

contribution) of at least 10 percent of the total project costs (all costs required to become operational, regardless of the source of funds, except for lines of credit and 504 loans) to be necessary for a Start-Up Business to operate on a sound financial basis. All 7(a) loans made to a Start-Up Business require a 10% equity injection based on the project cost; however, loans approved more than 90 days apart from each other are considered to be separate projects.;

ii) Changes of ownership: See Appendix 15: 7(a) Changes of Ownership

c) Source of Equity Injection: The following may be considered equity injection.

i) Standby Agreements - only debt that is on full standby (no payments of principal or interest for the term of the 7(a) loan) may be considered as equity for SBA's purposes. Lender must use SBA Form 155 or its own equivalent Standby Agreement form, and a copy of the note must be attached to the standby agreement. The standby debt may accrue interest and may be added to the standby debt and amortized after the 7(a) loan is paid in full. Standby Creditor must subordinate any lien rights in collateral securing the loan to Lender's rights in the collateral and take no action against Borrower or any collateral securing the Standby Debt without Lender's consent.

ii) Cash that is not borrowed, whether on the business's balance sheet or from other sources.

iii) Cash that comes from a personal loan where repayment can be demonstrated to come from a source other than the cash flow of the business (the salary paid to the owner by the business does not qualify).

iv) Grants that do not have repayment or clawback provisions during the life of the 7(a) loan.

v) Assets other than cash – An appraisal or other valuation by an independent third party is required if the valuation of the fixed assets is greater than the Net Book Value. A valuation of the fixed assets provided as part of a business valuation will not meet these requirements.

vi) Eligible prepaid expenses that the Lender has verified by obtaining paid invoices, canceled checks, or bank statements. Lender must retain copies of the documentation in the loan file.

(a) Expenses related to education, advisory servicers, or fees paid by the Applicant to an Agent are not eligible prepaid expenses and are

not considered equity.

vii) An equity investment not subject to an agreement to repay equity or make distributions to recover an investor's investment prior to release of the guaranty. Note: SBA will considers any investment subject to an agreement to repay equity or make distributions to recover an investor's investment prior to release of the guaranty (e.g., certain types of redeemable preferred stock)to be debt and not equity.

**b. Underwriting SBA Express Loans**

SBA has authorized SBA Express Lenders to make the credit decision without prior SBA review.

i. Lenders must use appropriate, prudent, and generally accepted industry credit analysis processes and procedures (which may include credit scoring), and these procedures must be consistent with those used for the Lender's similarly-sized, non-SBA guaranteed commercial loans. The requirements in Section A of this SOP apply to SBA Express loans.

ii. Lenders must not make an SBA Express loan that would be available on reasonable commercial terms from either the Lender itself or another source without an SBA guaranty. The credit analysis must include the factors demonstrating the Applicant does not have credit available elsewhere on reasonable commercial terms from non-Federal, non-State, non-local government sources, in accordance with Section A, Ch. 1, Para. H.;

iii. The credit analysis must demonstrate that there is a reasonable assurance of repayment.

iv. Lenders may use a business credit scoring model (such a model cannot rely solely on consumer credit scores) to assess character, reputation, and credit history of the applicant and/or repayment ability if they do so for their similarly-sized, non-SBA guaranteed commercial loans.

a) The business credit scoring model may only be used in addition to the Lender's appropriate, prudent, and generally accepted industry credit analysis and procedures. If used, the business credit scoring results must be documented in each loan file and available for SBA review.

b) Lenders must validate (and document) with appropriate and accepted statistical methodologies that their business credit scoring model is predictive of loan performance, and they must provide that documentation to SBA upon request.

c) Although SBLCs do not make non-SBA guaranteed loans, SBA has determined they may use credit scoring. SBLCs are required to provide credit scoring model validation to SBA on an annual basis.

v. For SBA Express loans, the credit decision, including how much to factor in a past bankruptcy or whether to require an equity injection, is left to the business judgment of the Lender. Also, if the Lender requires an equity injection and, as part of its standard processes for similarly-sized, non-SBA guaranteed commercial loans verifies the equity injection, it must do so for its SBA Express loans. While the credit decision is left to the business judgment of the Lender, early loan defaults will be reviewed by SBA pursuant to SOP 50 57.

vi. Lenders must also address other specifics, such as: franchise, license, dealer, or similar agreements and management agreements (unless the management agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory) to determine whether the management agreement makes the business an ineligible passive business.

3. Collateral

See Appendix 19: 7(a) Collateral Requirements Para. B.2-3.

See Section A, Ch. 5, Para. A. for guaranty requirements.

## D. SUBMISSION OF APPLICATION FOR GUARANTY

See Appendix 20: Submission of Application for Guaranty

## CHAPTER 3: 7(A) MANUFACTURERS' ACCESS TO REVOLVING CREDIT (MARC)

**Lenders must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.**

### A. ELIGIBILITY

Eligible small businesses are those that meet the eligibility requirements in SOP 50 10 8.1, Section A, and are engaged in the following industries/NAICS groups and National Industry Codes:

a. Manufacturing: NAICS sectors 31-33, where 31, 32, or 33 are the first 2 digits of the business' primary 6-digit NAICS code.

b. Wholesale: NAICS sector where 42 is the first 2 digits of the business' primary 6-digit NAICS code.

i. The following sectors are not eligible for financing under the MARC loan:

a) 423110 – Automobile and Other Motor Vehicle Merchant Wholesalers; or

b) 425120 – Wholesale Trade Agents and Brokers

c. Food Supply Chain: NAICS sector where 11 is the first 2 digits of the business' primary 6-digit NAICS code and the following National Industry Codes:

i. 445110 – Supermarkets and Other Grocery Retailers

ii. 493120 – Refrigerated Warehousing and Storage

iii. 493130 – Farm Warehousing and Storage

d. NAICS codes can be found at 13 CFR § 121.201, and a searchable database of industries and NAICS codes is located at North American Industry Classification System (NAICS) U.S. Census Bureau or NAICS.com. To determine the Applicant's primary NAICS code, see 13 § CFR 121.107.

1. Eligible Uses of Proceeds

Proceeds from a MARC program loan may only be used for the following purposes:

a. To support the working capital needs of the Applicant business; or

b. Refinancing debt in which the original purpose of the debt to be refinanced was for working capital purposes.

i. See Appendix 14: 7(a) Debt Refinancing Para. B.3. for MARC loan program specific guidance.

2. Ineligible Uses of Proceeds

   Proceeds must not be used for non-working capital debt refinance, changes of ownership, to pay delinquent withholding taxes or similar funds held in trust (e.g., state or local sales taxes), or for floor plan financing. MARC loan proceeds may not be used to pay a creditor in a position to sustain a loss.

   Although 7(a) MARC loans may not be used to fund a change of ownership, a 7(a) MARC loan may be made to a business at the same time as the change of ownership to support working capital needs. See change of ownership rules outlined in Appendix 15.

## B. LOAN TERMS AND CONDITIONS

1. Maximum Loan Amount varies by industry.
   a. Manufacturers (NAICS 31-33): $5,000,000.
   b. All other eligible industries: $2,000,000.
   c. To determine the maximum loan amount, the Lender must ensure the Borrower meets the debt service coverage requirements in the Underwriting section.
2. Maximum Loans to Businesses with Affiliates.

   13 CFR § 120.151 Lenders must determine whether the Applicant has any affiliates and document the results in their credit analysis. If affiliation exists, SBA's loan maximums apply to the Applicant, including all Affiliates, as if all were a single business.
3. Revolving Structure

   The loan must be a revolving loan.
   a. Revolving loans: May not be sold on the secondary market.
   b. Revolving MARC loans must contain a provision that allows the lender to begin amortizing the loan in the event that the Borrower does not meet the program requirements in Paragraph G, Post-Closing Requirements for Revolving Loans.
4. Disbursements

   Lenders must determine how to administer disbursements using the following methods:
   a. Structuring the loan for an open and revolving line of credit;
   b. Tiering the availability on an annual basis; or
   c. Administering the facility using a borrowing base certificate.

      For example, if the Lender anticipates a lower capital need in year one, the Lender may set a cap at the total amount the Borrower may draw for that period. The Lender may place additional controls over the disbursements and conditions, documented in the loan agreement. If the Borrower's working capital need increases after an annual review, if the annual review supports a higher loan

amount, Lenders may issue a new loan or request a loan increase (additional guaranty fees may be due, and the request for the loan increase must be made in accordance with the Servicing and Liquidation SOP 50 57).

5. Maximum Guaranty Amounts and Percentages: See Appendix 16: 7(a) Maximum Guaranty Amounts and Percentages Para. B.3.
6. Loan Maturities: See Appendix 17: 7(a) Loan Maturities Para B.4.
7. Interest Rates: See Appendix 18: 7(a) Interest Rate Requirements Para B.4.

SBA Quick Reference Chart:

| Product<br><br>**Manufacturers' Access to Revolving Credit (MARC)** | Interest Rate<br><br>**The maximum allowable fixed rate is available on SBA's Wiki page. Maximum variable rates are:** |
|---|---|
| Loans $50,000 or less | Cannot exceed Prime or SBA Optional Peg Rate + 6.5% |
| Loans $50,001 up to and including $250,000 | Cannot exceed Prime or SBA Optional Peg Rate + 6.0% |
| Loans $250,001 up to and including $350,000 | Cannot exceed Prime or SBA Optional Peg Rate + 4.5% |
| Loans $350,001 and greater | Cannot exceed Prime or SBA Optional Peg Rate + 3.0% |

## C. CREDIT STANDARDS

The policies that make up SBA's credit standards begin with the requirements outlined in 13 CFR §§ 120.101 and 120.150. This section provides procedural guidance as to what the Lender should or must consider when analyzing any request for financial assistance that will be guaranteed by SBA.

A Lender must analyze each application in a commercially reasonable manner, consistent with prudent lending standards. The cash flow of the Applicant is the primary source of repayment, not any expected recovery from the liquidation of collateral. Thus, if the Lender's financial analysis indicates that the Applicant lacks reasonable assurance of repayment in a timely manner from the business's cash flow, the loan request must be declined, regardless of the collateral available or outside sources of repayment.

1. Processing Methods

    a. **Non-delegated** – When a Lender submits a 7(a) MARC loan guaranty request under the non-delegated processing method, the Lender submits the application and supporting documents to SBA via the SBA Loan System. SBA will make the final determination regarding the eligibility and creditworthiness of the Applicant, including approval of the uses of proceeds, the adequacy of the collateral being pledged, the structure of the loan, and any equity contribution required from the

Applicant.

b. **PLP** – When a Lender submits a 7(a) MARC loan guaranty request under the Lender's PLP authority, the Agency does not review the Lender's analysis of the credit or structure of the loan or line of credit prior to issuing a loan number. The Lender must analyze creditworthiness in accordance with SBA Loan Program Requirements and properly document its file. The PLP Lender's analysis is subject to SBA's review and determination of adequacy when the Lender requests SBA to purchase its guaranty or when SBA is conducting lender oversight activities.

2. Underwriting

a. Lender's Credit Analysis:

The Lender's credit memorandum and analysis must address the Applicant's ability and likelihood to repay the loan from the cash flow of the business and past performance by documenting the following:

i. A description and history of the business, including:

a) Nature of the business, including NAICS code;

b) Length of time in business under current management;

c) Depth of management experience in the industry or a related industry;

d) Brief description of the business's management team, including the principal's involvement in the daily onsite management of the business or how the daily operations will be managed if the principals are not there on a daily basis.

e) If the daily operations will be handled under a management agreement, Lenders must obtain a copy of the management agreement (unless the management agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory), review it to determine if it results in an ineligible passive business, and retain in their loan file.

ii. Financial analysis of repayment ability:

a) The Lender must analyze the Applicant's repayment ability in accordance with 13 CFR § 120.191. The analysis must demonstrate that cash flow is sufficient to meet all debt obligations, including the proposed SBA loan, on a fully amortizing basis using the maximum loan amount and maturity approved.

The financial analysis for all Applicants:

i) Historical or projected cash flow analysis as outlined below:

(a) Calculation of earnings before interest, taxes, depreciation, and

amortization (EBITDA);

(b) Justification for additions and subtractions to cash flow such as the following:

(i) Unfunded capital expenditures;

(ii) Non-recurring income or expenses;

(iii) Expenses and distributions;

(iv) Distributions for S-Corp taxes;

(v) Rent payments;

(vi) Owner's Draw; and/or

(vii) Global cash flow analysis that includes assessment of the impact on cash flow to/from any affiliate business. Anticipated cash flow from rental income from the Project Property may be included in the global cash flow analysis;

(viii) The effect any affiliates may have on the ultimate repayment ability of the Applicant.

b) For cash flow projections, the Lender must calculate the debt service coverage and provide the assumptions supporting the projected cash flow coverage, including, as applicable:

i) Justification for revenue growth, i.e., new product lines, sales channels, and new production facilities;

ii) Justification for any reduction in expenses;

iii) A comparison to current industry trends.

iv) Spread of pro forma Business Balance Sheet (current business balance sheet adjusted for all changes in assets and liabilities as a result of the SBA loan, other debt, any required equity injection, and use of loan proceeds);

v) Ratio calculations (based on the pro-forma Balance Sheet and historical and projected Income Statements) for the following financial ratio benchmarks: Current Ratio, Debt/Tangible Net Worth, Debt Service Coverage, and any other ratios the Lender considers significant for the business/ industry (e.g., inventory turnover, receivables turnover, and payables turnover, etc.) including discussion of Lender's comparison to industry trends;

vi) Analysis of Borrower's working capital adequacy.

c) Assessment of collateral adequacy in accordance with Appendix 19

Para. B.4; and

d) Insurance Requirements, including:

i) Life Insurance – on whom and how much. If life insurance will not be required, provide justification.

ii) Business hazard & liability insurances.

e) Lender's rationale for recommending approval, including a discussion and analysis of the following:

i) The factors demonstrating the Applicant does not have credit available elsewhere on reasonable commercial terms from non-Federal, non-State, non-local government sources in accordance with SOP 50 10 8.1, Section A, Ch. 1, Para. H.

ii) Competition;

iii) Seller financing;

iv) Stand-by agreements;

v) 90+ day delinquencies;

vi) Trade disputes and/or;

vii) Federal, State, or local citations which would preclude the Applicant from normal business operations;

viii) Discussion of any liens, judgments, bankruptcy filings, or pending litigation, including divorce proceedings;

ix) If the application involves a franchise (as defined by FTC), the Lender must review any credit information provided, such as the number of failed franchisees and cash flow projections provided by the franchisor.

x) Discussion of other relevant information.

iii. Existing Businesses - Historical DSCR Analysis:

a) The Lender must evaluate repayment ability using the Applicant's historical financial performance, including the three most recent fiscal years of financial statements (or tax returns) and current interim financial statements.

i) The analysis must:

(a) Include all existing and proposed debt obligations;

(b) Calculate total debt service coverage after inclusion of the SBA loan;

(c) Be based on the amortizing loan term that does not exceed ten (10) years and uses the maximum loan amount approved;

(d) The Applicant must demonstrate a minimum debt service coverage (DSC) ratio of 1.15:1 based on historical performance. Global DSC ratio must be at least 1.0:1, and

(e) If the most recent full year and interim financial statements do not demonstrate DSC ratio of at least 1.15:1, the Lender must obtain and analyze two years of projections in accordance with the paragraph below.

iv. Start-Ups, New Businesses, and Transactions Requiring Projections:

a) For start-ups, new businesses, changes of ownership, or when historical performance is insufficient, the Lender must base repayment ability on projected financial performance.

i) The projections must:

(a) Cover a minimum of two years;

(b) Include detailed and supportable assumptions;

(c) Be based on the amortizing loan term that does not exceed ten years, using the maximum loan amount;

(d) Include the total debt load of the business, including the proposed SBA loan;

(e) The projections must demonstrate that the Applicant will achieve a DSC ratio of at least 1.15:1 within one year from the date of loan disbursement;

(f) Global debt service coverage must be at least 1:1;

(g) For Global DSC, the Applicant must provide a quarterly cash flow analysis for a period of 24 months;

(h) The Lender must document and support any reliance on projections, including justification for variance from historical performance, if applicable. To perform a complete analysis of debt service, it is important for a Lender to obtain a current debt schedule prepared by the Applicant, including any shareholder debt.

v. DSC Ratio Calculation Requirements for all Applicants:

a) The DSC Ratio Calculation must include all business debt (existing and proposed);

b) The calculation must be based on a fully amortizing repayment structure;

c) The maximum loan amount and maturity approved must be used; and

d) The analysis must demonstrate ongoing repayment ability and sustainability of cash flow.

b. Equity requirements (13 CFR § 120.150):

i. Depending on whether the loan is processed on a non-delegated or PLP basis, the Lender or SBA must determine that there is sufficient invested equity. To do this, the Lender (for PLP lenders) or SBA (for non-delegated lenders) must determine if the equity position and the pro forma debt-to-worth are acceptable based on the factors related to the type of business, experience of management, and the level of competition in the market area. The Lender must include in its credit memorandum a detailed discussion of the equity position (net worth) and any required equity injection. Unlike Standard 7(a) and 7(a) Small loans, 7(a) MARC loans do not have a minimum required equity injection based on use of proceeds.

3. Collateral

See Appendix 19: 7(a) Collateral Requirements Para. B.4.

See SOP 50 10 8.1, Section A, Ch. 5, Para. A. for guaranty requirements.

## D. FEES THAT THE LENDER MAY CHARGE THE BORROWER

See SOP 50 10 8.1, Ch. 4 for requirements for ethics, fees, and Agents.

In addition to the fees in SOP 50 10 8.1, Section A, Ch. 4, Para. C.2, at the time of the annual review, the Lender may charge an extraordinary servicing fee of up to 50 basis points (0.50%) based on the maximum loan amount. Note: Lenders may not charge the 50 basis point fee on loans that are not revolving (i.e., revolving loans that have been termed out).

Asset-based lines: Lenders may administer MARC loans as an asset-based line (e.g., similar to the 7(a) Working Capital CAPLines program or based on the Lender's policies for its similarly-sized non-SBA guaranteed asset-based lines). When administering the MARC loan as an asset-based line, the Lender may charge an annual extraordinary servicing fee not to exceed 200 basis points (2%) of the outstanding balance. For MARC Loans, the Lender may assess this extraordinary servicing fee independent of fees based on the Lender's policies for its similarly sized non-SBA guaranteed asset-based lines of credit by the institution.

For asset-based lines, the Lender may only charge one category of extraordinary servicing fee, either the traditional extraordinary service fee not to exceed 2% or the 50 basis point fee calculated on the maximum loan amount.

For all MARC loans, SBA has granted a blanket waiver on the Lender's requirement to seek prior written approval when assessing either category of the extraordinary service fee outlined in this section.

## E. DESIGNATING 7(A) MARC LOANS IN THE SBA LOAN SYSTEM

Lenders must indicate that these loans are 7(a) MARC loans when entering the application into the SBA Loan System.

## F. SUBMISSION OF APPLICATION FOR GUARANTY: SEE APPENDIX 20: SUBMISSION OF APPLICATION FOR GUARANTY

Lenders that do not have delegated PLP authority: Must submit applications to SBA via the SBA Loan System for SBA approval under non-delegated procedures.

Lenders with PLP delegated authority: Lenders with PLP delegated authority are required to process 7(a) MARC loans using their PLP authority.

## G. POST-CLOSING REQUIREMENTS FOR REVOLVING LOANS

Beginning no later than the end of the second year (24 months from approval):

1. For revolving loans, Lenders must conduct an annual review of business financials to determine whether the line may continue to revolve for an additional year or whether the facility should be termed out. This review must include an analysis of the previous year-end financial performance and the most recent interim statement available. This review may coincide with the Lender's annual renewal process for the loan.

   The Lender must use a combination of factors for the decision consistent with its similarly-sized, non-SBA guaranteed commercial lines of credit, or, if the Lender does not make similarly-sized non-guaranteed loans, consistent with prudent lending standards. The Lender's analysis must assume full use of the revolving line of credit and must include at a minimum;

   a. Cash flow analysis to determine the adequacy, duration, and dependability of cash flow;

   b. Owner/Guarantor analysis, except Supplemental Guarantors;

   c. Documentation that the Borrower:

      i. Can support a debt service coverage ratio of at least 1.10:1. Debt service coverage calculation must be based on the full debt service of the business, including the debt service for the 7(a) MARC loan, on a fully amortizing basis using the maximum loan amount and maturity approved.

      ii. Has no bankruptcy filings against the company.

      iii. Is current at the time of the review (meaning total interest due to date has been paid), and

iv. Maintains sufficient collateral as described in Appendix 19, Para. B.4.

d. If each of the above requirements are met, the line may continue to revolve.

e. If the above requirements are not met, the line must be converted to a fully amortizing term loan with a zero balance at loan maturity.

f. The Lender may require the line to convert to a fully amortizing term loan at any point, if the Lender deems it necessary, based on prudent lending criteria.

g. Once the loan has been converted to a term loan, the Lender may not make further disbursements on the line.

h. In the event that the Lender discovers that proceeds were used to acquire fixed assets under the revolving portion of the loan, the Lender has the ability to convert the portion of the loan to a fully amortizing term loan (which may be a 7(a) term loan) in order to preserve the availability of the revolving line of credit for eligible working capital purposes.

i. Disbursements: See Disbursements in this Chapter above.

## H. SERVICING OPTIONS

1. Lenders must follow SOP 50 57 and the Servicing and Liquidation Actions 7(a) Lender Matrix for servicing and liquidation requirements. Additionally, Lenders may extend the loan maturity by up to 10 years to help a Borrower remain current or, if a Borrower becomes delinquent, to help the Borrower regain currency. In such cases, the loan must be converted to a fully amortizing loan with a zero balance at loan maturity.
2. Lenders may also defer payments.
    a. Revolving loans may be deferred for up to 6 months.

# CHAPTER 4: 7(A) CAPLINES

13 CFR § 120.390

Lines of credit under CAPLines finance the short-term operating capital needs (revolving and non-revolving) of eligible small businesses.

## Lenders must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.

## A. ELIGIBILITY AND ELIGIBLE USES OF PROCEEDS FOR ALL CAPLINES

CAPLines proceeds can be used to finance the cyclical, recurring, or other identifiable short-term operating capital needs of small businesses. Proceeds can be used to create current assets or to provide financing against the current assets that already exist.

**In order to be eligible for any of the CAPLines subprograms, the Applicant must be eligible under the requirements identified in Section A, AND what is listed below for each subprogram:**

1. Working Capital CAPLines

   **a. Eligibility**

   To be eligible for a Working Capital CAPLine, the Applicant must generate accounts receivable (not notes receivable), and/or have inventory.

   **b. Eligible Uses of Proceeds**

   i. Borrowers may only use the loan proceeds for short-term working capital/ operating needs. Proceeds must not be used to pay delinquent withholding taxes or similar funds held in trust (e.g., state or local sales taxes), or for floor plan financing. In the event that Working Capital CAPLine proceeds are used to acquire fixed assets, Lender must refinance the portion of the line used to acquire the fixed asset into an appropriate term facility no later than 90 days after the Lender discovers that the line was used to finance a fixed asset.

   ii. Borrowers may be Exporters engaged in Export Transactions. Loan proceeds may be used for Domestic-to-Foreign Exports, and Foreign-to-Foreign Exports. Note: See Appendix 16 Para. B.4 for maximum guaranty amounts and percentages for CAPLines to Exporters, which are different than those for EWCP.

   iii. Debt Refinancing under Working Capital CAPLines: See Appendix 14: 7(a) Debt Refinancing Requirements Para. B.4.

2. Contract CAPLines

   **a. Eligibility**

To be eligible for a Contract CAPLine, the Applicant must:

i. Be able to demonstrate the ability to operate profitably based upon the prior completion of similar contracts;

ii. Possess the overall ability to bid, accurately project costs, and perform the specific type of work required by the contract(s); and

iii. Have the financial capacity and technical expertise to complete the contract on time and at a profit.

**b. Eligible Uses of Proceeds**

i. The contractor must use loan proceeds only to finance the costs of one or more specific contracts, including overhead or general and administrative expenses, allocable to the specific contract(s).

ii. Contract CAPLine proceeds may not be used:

a) For permanent working capital;

b) To acquire fixed assets;

c) To pay delinquent taxes or similar funds held in trust (directly or indirectly);

d) To refinance existing debt;

e) To finance a contract in which significant performance has already begun;

f) To finance a change of ownership;

g) For floor plan financing; or

h) To cover any mark-up or profit.

c. Advances of loan proceeds financing performance of one contract or sub-contract under a master agreement may not be used to finance the performance of another contract or sub-contract.

d. Progress payments or proceeds received in the performance of a contract or sub-contract financed with this line must not be applied in repayment of a different contract or sub-contract. Funding and payment applications must be accounted for in conjunction with the specific contract or sub-contract to which they relate.

e. A single Contract CAPLine may be used to fund a single or multiple contracts. Once the overall line amount has been approved by SBA, the lender may advance against additional contracts without SBA approval, provided that the Borrower and Lender are in compliance with all terms. The contracting parties, as a result of a properly executed change order, may agree to increase the contract price subsequent to the approval of the Contract CAPLine. In such event, if the overall

line amount needs to be increased, the Lender must comply with Ch. 6, Para. B.2, For SBA loans that have been fully disbursed, in this Section below to obtain SBA's approval of the increase in the line. The contracting parties, as a result of a properly executed change order, also may agree to decrease the contract price subsequent to the approval of the Contract CAPLine and/or after a progress advance was made. In such event, the lender must ensure the Borrower is aware that the next future advance or future advances, if necessary, will be at the decreased amount.

3. Seasonal CAPLines

**a. Eligibility**

To be eligible for a Seasonal CAPLine, the Applicant must:

i. Have been in operation for at least 12 calendar months; and

ii. Be able to demonstrate a definite pattern of seasonal activity.

**b. Eligible Uses of Proceeds**

i. Borrowers must use the loan proceeds solely to finance the seasonal increases of accounts receivable and inventory (or in some cases associated increased labor costs).

ii. Funds must not be used to:

a) Maintain activity during the slow periods of the business's cycle; or

b) Refinance existing debt.

4. Builders CAPLines

13 CFR §§ 120.391 – 120.397

Builders CAPLines provide financing to small general contractors to construct or rehabilitate residential or commercial property for resale. This program provides an exception under specified conditions to the general rule against financing investment property. "Construct" and "rehabilitate" mean only work done on-site to the structure, utility connections, and landscaping.

**a. Eligibility**

To be eligible for a Builders CAPLine, the Applicant must:

i. Be a construction contractor or homebuilder with demonstrated managerial and technical ability in profitable construction or renovation;

ii. Must either perform the construction/renovation work or manage the job with at least one supervisory employee on the job site during the entire construction phase;

iii. Renovations must be "prompt and significant." Construction must begin within a reasonable time after loan approval and the cost of renovation must equal or exceed one-third (1/3) of the purchase price of the property. The cost of renovation of buildings already owned by the Applicant must equal or exceed one-third (1/3) of the fair market value at the time of loan application;

iv. Demonstrate a successful performance record in bidding and completing construction/renovation at a profit within the estimated construction period, and the prior successful performance must have been of comparable type and size to the proposed project (prior experience in single family construction is not comparable to high-rise apartment construction); and

v. Be able to demonstrate prior prompt payments to suppliers and subcontractors.

**b. Eligible Uses of Proceeds**

13 CFR §§ 120.394 and 120.397

i. Borrowers must use the loan proceeds solely for direct expenses related to the construction and/or "substantial" renovation costs of a specific eligible project (residential or commercial buildings for resale), including labor, supplies, materials, equipment rental, direct fees (building permits, interim disbursement inspection fees, etc.), utility connections (above or below ground), construction of septic tanks, and landscaping. ("Substantial" means rehabilitation expenses of more than one-third of the purchase price or fair market value at the time of application.)

ii. Proceeds paid to a subcontractor can include the subcontractor's profit. The cost of land is eligible if the land cost does not exceed 33 percent of the project cost. Up to 5% of the project cost can be allocated for improvements that benefit all properties in a subdivision, such as streets, curbs, sidewalks, or open spaces.

iii. Proceeds must not be used to:

a) Purchase vacant land for possible future construction;

b) Operate or hold rental property for future rehabilitation; or

c) Refinance existing debt.

c. A single line may be used to fund multiple projects. Once the overall line amount has been approved by SBA, the Lender may advance against additional projects without SBA approval, providing the Borrower and Lender are in compliance with all terms.

d. SBA may allow the finished property to be rented pending sale only in cases where the rental will enhance the ability to sell the property.

e. The final sale of the property must be an arm's length transaction with legal transfer to an unaffiliated third party.

## B. LOAN TERMS AND CONDITIONS FOR ALL CAPLINES

1. Maximum Loan Amount

   a. The maximum loan amount is $5,000,000.

   b. Maximum Loans to Businesses with Affiliates

      13 CFR § 120.151 Lenders must determine whether the Applicant has any affiliates and document the results in their credit analysis. If affiliation exists, SBA's loan maximums apply to the Applicant, including all affiliates, as if all were a single business.

   c. Working Capital CAPLines

      To determine the maximum line amount for loans not administered through the use of a Borrowing Base Certificate, the Lender must either:

      i. Follow its established policies and procedures used on its similarly-sized, non-SBA guaranteed commercial lines of credit; or

      ii. Use the following formula:

         a) Divide Prior Year Net Sales by 365 to calculate the daily sales figure;

         b) Multiply Daily Sales figure by number of days to finance (whatever number is the business sales cycle)

      The result will be the estimated working capital needs. For loans administered using a borrowing base Certificate, the Lender may determine the line size based on the availability of collateral and the Borrower's expected working capital need.

   d. Contract CAPLines

      i. For single contract financing with a single payment, the loan amount is equal to the sum of the costs of the contract, as evidenced by the project cost schedule.

      ii. For a single contract with multiple payments, the loan amount is the amount projected by the Borrower necessary to cover 20% over the greatest cash deficit projected for the subject contract. This permits the line to revolve within the term of the contract.

      iii. For multiple contract financing, the master note amount is equal to the sum of the costs of all contracts to be financed under the CAPLine, as evidenced by the project cost schedules. For future projects not yet identified, at the time the contract is obtained all costs by line item should be identified. The

amount of the sub-note for each specific contract should equal the total costs of that contract.

e. Seasonal CAPLines

The loan amount is based on the cash flow projections. The amount should correlate to the costs of the seasonal buildup of inventory and/or receivables.

f. Builders CAPLines

i. For a non-revolving loan, the loan amount is based on the written proposal of costs (not anticipated selling price) provided by the applicant for a single project.

**ii.** For a revolving loan, the master note amount is based on the cash flow projections provided by the applicant for ALL work to be performed by the small business (not just a specific project). The amount of a sub-note (for each specific project) is based on the written proposal of costs (not anticipated selling price) provided by the Applicant for that particular project.

2. Maximum Guaranty Amounts and Percentages: See Appendix 16: 7(a) Maximum Guaranty Amounts and Percentages Para. B.4.
3. Loan Maturities: See Appendix 17: 7(a) Loan Maturity Requirements Para B.5.
4. Interest Rates: See Appendix 18: 7(a) Interest Rate Requirements Para. B.5.

SBA QUICK REFERENCE CHART: Maximum Interest Rates Allowed

| **Product**<br><br>**7(a) CAPLines** | **Interest Rate**<br><br>**The maximum allowable fixed rate is available on SBA's Wiki page. Maximum variable rates are:** |
|---|---|
| Loans $50,000 or less | Cannot exceed Prime or SBA Optional Peg Rate + 6.5% |
| Loans $50,001 up to and including $250,000 | Cannot exceed Prime or SBA Optional Peg Rate + 6.0% |
| Loans $250,001 up to and including $350,000 | Cannot exceed Prime or SBA Optional Peg Rate + 4.5% |
| Loans $350,001 and greater | Cannot exceed Prime or SBA Optional Peg Rate + 3.0% |

## C. CREDIT STANDARDS FOR ALL CAPLINES

The policies that make up SBA's credit standards begin with the requirements outlined in 13 CFR §§ 120.101 and 120.150. This section provides procedural guidance as to what the

Lender should or must consider when analyzing any request for financial assistance that will be guaranteed by SBA.

A Lender must analyze each application in a commercially reasonable manner, consistent with prudent lending standards. The cash flow of the Applicant is the primary source of repayment. In CAPLines, the cash flow of the Applicant may include the conversion of assets to cash. Thus, if the Lender's financial analysis demonstrates that the Applicant lacks reasonable assurance of repayment in a timely manner from the cash flow of the business, the loan request must be declined, regardless of the collateral available or outside sources of repayment.

1. Processing Methods

    a. Non-delegated – When a Lender submits a CAPLine loan guaranty request under the non-delegated processing method, the Lender submits the application and supporting documents to SBA. SBA will make the final determination as to the eligibility and creditworthiness of the Applicant, including approving the uses of proceeds, the adequacy of the collateral being pledged, the structure of the loan and any equity contribution to be required from the Applicant.

    b. Delegated – When a Lender submits a CAPLine loan guaranty request under the Lender's PLP authority, the Agency does not review the Lender's analysis of the credit or structure of the loan or line of credit prior to issuing a loan number. The Lender must analyze credit worthiness in accordance with SBA Loan Program Requirements and properly document its file. The PLP Lender's analysis is subject to SBA's review and determination of adequacy when the Lender requests SBA to purchase its guaranty or when SBA is conducting lender oversight activities.

2. Underwriting

    a. Lender's Credit Analysis:

        The Lender's credit memorandum and analysis must address the Applicant's ability and likelihood to repay the loan from the cash flow of the business and past performance by documenting the following:

        i. A description and history of the business, including:

            a) Nature of the business;

            b) Length of time in business under current management;

            c) Depth of management experience in the industry or a related industry;

            d) Brief description of the business's management team including principal's involvement in the daily onsite management of the business or how the daily operations will be managed if the principals are not there on a daily basis.

e) If the application involves a franchise (as defined by FTC), the Lender must review any credit information provided, such as the number of failed franchisees and cash flow projections provided by the franchisor). Lender must review any management agreement (unless the management agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory) to determine if it results in an ineligible passive company;

ii. Financial analysis of repayment ability:

a) For existing businesses based on the three most recent years of historical financial information (tax returns or balance sheet with debt schedule and income statement) plus an interim financial statement. (13 CFR § 120.191)

b) For new businesses, based on detailed projections, including the supporting assumptions which reflect positive cash flow within 2 years.

c) The financial analysis for all Applicants must address the following as applicable:

i) Historical cash flow for existing businesses, that demonstrates total debt service coverage after the SBA loan; if the historical cash flow from the most recent full year and the interim financial statements do not show sufficient debt service coverage, Lender must obtain from the Applicant and analyze 2 years of detailed projections including the supporting assumptions justifying relying on projections instead of historical performance;

ii) Calculation of operating cash flow (OCF) defined as earnings before interest, taxes, depreciation, and amortization (EBITDA);

iii) Justification for additions and subtractions to cash flow such as the following:

(a) Unfunded capital expenditures;

(b) Non-recurring income;

(c) Expenses and distributions;

(d) Distributions for S-Corp taxes;

(e) Rent payments;

(f) Owner’s Draw; and/or

(g) Global cash flow analysis that includes assessment of impact on cash flow to/from any affiliate business.

iv) The effect any affiliates may have on the ultimate repayment ability of the Applicant.

iii. Debt Service (DS) is defined as the future required principal and interest payments on all business debt inclusive of new SBA loan proceeds. The Applicant's debt service coverage ratio (OCF/DS) must be equal to or greater than 1.15 on a historical and/or projected cash flow basis and 1:1 on a global basis. To perform a complete analysis of debt service, it is important for a Lender to obtain a current debt schedule prepared by the Applicant, including any shareholder debt.

iv. For cash flow projections, the Lender must calculate the debt service coverage and provide the assumptions supporting the projected cash flow coverage, including as applicable:

a) Justification for revenue growth, i.e., new product lines, sales channels, and new production facilities;

b) Justification for any reduction in expenses; and

c) A comparison to current industry trends.

v. Spread of pro-forma Business Balance Sheet (current business balance sheet adjusted for all changes in assets and liabilities as a result of the SBA loan, other debt, any required equity injection and use of loan proceeds);

vi. Ratio calculations (based on the pro-forma Balance Sheet and historical and projected Income Statements) for the following financial ratio benchmarks: Current Ratio, Debt/Tangible Net Worth, Debt Service Coverage, and any other ratios the Lender considers significant for the business/ industry (e.g., inventory turnover, receivables turnover, and payables turnover, etc.) including discussion of Lender's comparison to industry trends;

vii. Analysis of working capital adequacy, at a minimum over the next 12 months;

viii. Insurance Requirements, including:

a) Life Insurance – on whom and how much. If life insurance will not be required, provide justification.

b) Business hazard & liability insurances.

ix. Explanation of and justification for the refinancing of any debts as part of the loan request, along with supporting documentation, in accordance with the debt refinancing requirements in Appendix 14. In addition, Lender must include a written explanation for any late payments over the past 12 months.

x. Lender's rationale for recommending approval, including a discussion and analysis of the following:

a) The factors demonstrating the Applicant does not have credit available elsewhere on reasonable commercial terms from non-Federal, non-State, non-local government sources, in accordance with Section A, Ch. 1, Para. H, Credit Not Available Elsewhere;

b) Competition;

c) Seller financing;

d) Stand-by agreements;

e) 90+ day delinquencies;

f) Trade disputes and/or;

g) Federal, State, or local citations which would preclude the Applicant from normal business operations;

h) Discussion of any liens, judgments, bankruptcy filings or pending litigation including divorce proceedings; and

i) Discussion of other relevant information (for example, if the application involves a franchise (as defined by FTC), Lender must review any credit information provided such as the number of failed franchisees and cash flow projections provided by the franchisor).

b. Equity requirements (13 CFR § 120.150):

i. Depending on whether the loan is processed on a non-delegated or PLP basis, the Lender or SBA must determine that there is sufficient invested equity. To do this, the Lender (for PLP loans) or SBA (for non-delegated loans) must determine if the equity position, any required equity contribution, and the pro forma debt-to-worth are acceptable based on the factors related to the type of business, experience of management and the level of competition in the market area. The Lender must include in its credit memorandum a detailed discussion of the equity position (net worth) and any required equity injection. (See Ch. 6, Para. D., Loan Closing and Disbursement, of this Section for requirements concerning documenting and verifying equity injection.)

ii. Minimum equity injection requirements for certain Applicants or loans:

Start-Up Businesses – At a minimum, SBA considers an equity injection (Applicant contribution) of at least 10 percent of the total project costs (all costs required to become operational, regardless of the source of funds, except for lines of credit and 504 loans) to be necessary for a Start-Up Business to operate on a sound financial basis. SBA considers a business to

be a "start-up" for the purpose of determining equity injection requirements if it has been in operation (i.e., generating revenue from intended operations) for 1 year or less;

iii. Equity Injection: The following may be considered equity injection.

a) Standby Agreements - only debt that is on full standby (no payments of principal or interest for the term of the 7(a) loan) may be considered as equity for SBA's purposes. Lender must use SBA Form 155 or its own equivalent Standby Agreement form, and a copy of the note must be attached to the standby agreement. The standby debt may accrue interest and may be added to the standby debt and amortized after the 7(a) loan is paid in full. Standby Creditor must subordinate any lien rights in collateral securing the loan to Lender's rights in the collateral and take no action against Borrower or any collateral securing the Standby Debt without Lender's consent.

b) Cash that is not borrowed, whether on the business's balance sheet or from other sources.

c) Cash that comes from a personal loan where repayment can be demonstrated to come from a source other than the cash flow of the business (the salary paid to the owner by the business does not qualify).

d) Grants that do not have repayment or clawback provisions during the life of the 7(a) loan.

e) Assets other than cash – An appraisal or other valuation by an independent third party is required if the valuation of the fixed assets is greater than the Net Book Value. A valuation of the fixed assets provided as part of a business valuation will not meet these requirements.

f) Eligible prepaid expenses that the Lender has verified by obtaining paid invoices, canceled checks, or bank statements. Lender must retain copies of the documentation in the loan file.

i) Expenses related to education, advisory servicers, or fees paid by the Applicant to an Agent are not eligible prepaid expenses and are not considered equity.

g) An equity investment not subject to an agreement to repay equity or make distributions to recover an investor's investment prior to release of the guaranty. Note: SBA will considers any investment subject to an agreement to repay equity or make distributions to recover an investor's investment prior to release of the guaranty (e.g., certain types of redeemable preferred stock) to be debt and not equity.

3. Collateral

   See Appendix 19: 7(a) Collateral Requirements Para. B.5.

   See Section A, Ch. 5, Para. A. for guaranty requirements.

## D. FEES THAT THE LENDER MAY CHARGE THE BORROWER

See Section A., Ch. 4 for requirements for ethics, fees, and Agents.

1. In addition to the fees in Section A., Ch. 4, Para. C.2, at the time of the annual review, Lender may charge extraordinary servicing fees in excess of 2% for Working Capital CAPLine loans that are disbursed based on a Borrowing Base Certificate. The fees charged must be reasonable and prudent based on the level of extraordinary effort required and must not be higher than the fees charged on the Lender's similarly-sized, non-SBA guaranteed commercial loans.

## E. SUBMISSION OF APPLICATION FOR GUARANTY FOR ALL CAPLINES

See Appendix 20: Submission of Application for Guaranty

## CHAPTER 5: 7(A) EXPORT TRADE FINANCE

SBA has three core 7(a) international trade finance programs that support small business Exporters and Export Transactions.

Export Express Loan Program: The Export Express Loan Program guarantees smaller dollar revolving lines of credit or term loans to support small business concerns that wish to develop the export side of their business. It offers many of the streamlined features of SBA Express while providing a higher guarantee to mitigate international credit risk.

Export Working Capital Program: (EWCP): Under the EWCP, SBA guarantees short-term working capital loans made by participating lenders to small business Exporters.

International Trade Loan Program: Under the International Trade Loan Program, SBA guarantees term loans to improve the competitive position of small business concerns that are existing Exporters or are developing new export markets. SBA also guarantees term loans to improve the competitive position of any small business concerns adversely affected by import competition.

## A. EXPORT EXPRESS

The Export Express Loan Program guarantees smaller dollar revolving lines of credit or term loans to support small business concerns that wish to develop the export side of their business. It offers many of the streamlined features of SBA Express while providing a higher guarantee to mitigate international credit risk.

**Lenders must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.**

1. Eligibility and Eligible Uses of Proceeds for Export Express

   In addition to the core requirements identified in Section A, eligibility for Export Express is limited to businesses that have been in operation, although not necessarily as Exporters, for at least 12 full months. However, Applicants that have been in operation for less than 12 months are eligible if both of the following conditions are met:

   - The Applicant's key personnel have clearly demonstrated Export Transaction expertise and substantial previous successful business experience; and
   - The Lender processes the Export Express loan using conventional commercial loan underwriting procedures and does not rely solely on credit scoring or credit matrices to approve the loan. Non-bank Lenders that do not have a conventional loan portfolio must submit their underwriting procedures to the Office of Credit Risk Management for written approval prior to making an Export Express loan.

   Evidence of compliance with both of these requirements must be retained by the Lender in its file.

   a. Export Express loans must be used for an export development activity, which includes the following:

      i. Translation of product brochures or catalogues for use in markets outside the United States;

      ii. Obtaining a general line of credit for Export Transaction purposes (as a normal course of business, the Borrower may use portions of the line of credit for domestic purposes, as long as no less than 70% of the line of credit will be used for export purposes);

      iii. Performing a service contract from buyers located outside the United States;

      iv. Obtaining transaction-specific financing associated with completing Export Transaction orders;

      v. Acquiring, constructing, renovating, modernizing, improving, or expanding a production facility or equipment to be used in the United States in the production of goods or services for Export Transactions;

vi. Providing term loans and other financing to enable a small business concern, including an export trading company and an export management company, to develop a market outside the United States

vii. A 7(a) loan may not be used to refinance a debt owed to a Small Business Investment Company (SBIC) or a New Markets Venture Capital Company 13 CFR § 120.130(b).

viii. The payment of trade payables is not considered to be debt refinancing.

b. Debt Refinancing: See Appendix 14: 7(a) Debt Refinancing Requirements Para. B.6.

c. Change of Ownership: See Appendix 15: 7(a) Changes of Ownership

d. Loan proceeds may not be used to:

i. Finance operations outside of the United States, except for the marketing and/or distribution of products/services exported from the United States; or

ii. Refinance existing SBA-guaranteed loans except as permitted under Appendix 14: 7(a) Debt Refinancing Requirements Para. B.6.

iii. Fund a Change of Ownership transaction. Please see Appendix 15 for rules on Change of Ownership financing.

e. When an Export Express loan finances specific export transactions (including indirect exports) under Paragraph 1.a.i.v. or vi. above, the Lender must determine if U.S. companies are authorized to conduct business with the Parties and the country(ies) to which the goods or services will be shipped. Lenders must check Ex-Im Bank's Country Limitation Schedule, which can be found on Ex-Im Bank's website at www.exim.gov/tools-for-exporters/country-limitation-schedule or is available from SBA's Office of International Trade. The Lender also must check the Department of Treasury Office of Foreign Assets Control (OFAC) sanctions lists, which can be found at sanctionssearch.ofac.treas.gov/.

i. For federally-regulated Lenders, compliance with the procedures required by the Lender's Federal Financial Institution Regulator will constitute compliance with the above referenced OFAC requirement.

ii. For SBA Supervised Lenders, Lender must check the OFAC sanctions lists prior to first disbursement of funds on each specific export transaction. A loan may not be made to a business that directly or indirectly exports to a foreign country which is listed as a prohibited country (Note # 7 on the Country Limitation Schedule), or if the transaction would be prohibited under any of the sanctions programs administered by OFAC.

f. Documentation required: SBA requires the Lender to obtain information from the Borrower pertaining to the use of proceeds and its projected impact on the

Borrower's export sales and retain that documentation in its loan file. The Applicant must provide documentation regarding the following items (this may be in the form of a general business plan, an attachment to the loan application or on a Lender-developed questionnaire):

i. Estimated total export sales the loan will support;

ii. A brief description of the business' product or service which will be exported;

iii. An explanation of how the loan proceeds will enable the business to enter a new export market or expand in an existing export market;

iv. The countries to which the business will export; and

v. An estimate of the Borrower's export sales for the 12 month period following the date of the loan application.

2. Other Restrictions that apply to Export Express Loans

For purposes of clarification, small businesses in the following NAICS Industry Subsector Codes cannot be financed using an Export Express Loan, but may be financed using other SBA 7(a) financial assistance:

a. NAICS Industry Subsector Code 721 (Accommodation)

b. NAICS Industry Subsector Code 457 (Gasoline Stations).

3. Loan Terms and Conditions for Export Express

**a. Maximum Loan Amount**

i. The maximum loan amount is $500,000 (gross).

ii. Maximum Loans to Businesses with Affiliates

13 CFR § 120.151 Lenders must determine whether the Applicant has any affiliates and document the results in their credit analysis. If affiliation exists, SBA's loan maximums apply to the Applicant, including all affiliates, as if all were a single business.

**b. Maximum Guaranty Amounts and Percentages**

The maximum dollar amount outstanding of SBA's guaranty to any one business (including affiliates) must not exceed $3,750,000. SBA considers an EPC and an OC to be "one business" for this purpose. When calculating the maximum guaranty percentage available to a Borrower and its affiliates, the Lender must include the approved loan amount for a revolving line of credit. The SBA's guaranty is also known as the "SBA share" or "guaranteed portion."

i. Multiple Export Express loans are allowed up to the program maximum loan amount ($500,000 gross for Export Express). The guaranteed amount of all

Export Express loans counts toward the $3,750,000 maximum SBA exposure that may be outstanding for all SBA loans to a Borrower and its affiliates at any one time.

ii. If multiple Export Express loans are approved within 90 days of each other, and the combined gross loan amount of all the Export Express loans approved in that time frame to any one Borrower (including affiliates) exceeds $350,000, then the maximum guaranty percentage on the second loan must be reduced accordingly so the combined guaranty is no more than 75% (subject to the $3,750,000 guaranty amount limit).

iii. The maximum guaranty percentage is:

a) 90% for loans of $350,000 or less; and

b) 75% for loans over $350,000 up to $500,000.

iv. Combination of 7(a) and 504 loans

a) When an Applicant applies for any combination of 7(a) and 504 loans, the order in which the loans are approved determines the maximum loan and guaranty amount available. Because the 7(a) loan has a lower maximum guaranteed amount, the 7(a) loan should be processed and approved first.

b) Lenders must advise the SBA processing centers that there is a companion 504 application to ensure the 7(a) loan is processed and approved prior to the 504 loan application being processed and approved.

v. Zero Percent Guaranty Cannot be Provided for Ineligible Purposes:

A 7(a) loan cannot include proceeds for an ineligible purpose or have any portion of the loan made to an ineligible business and no part of an SBA 7(a) loan may be guaranteed at zero percent.

**c. Loan Maturities: See Appendix 17: Loan Maturity Requirements Para. B.6.**

**d. Interest Rates: See Appendix 18: 7(a) Interest Rate Requirements Para. B.6.**

SBA QUICK REFERENCE CHART: Maximum Interest Rates Allowed

| Product<br><br>Export Express Loans | Interest Rate<br><br>The maximum allowable fixed rate is available on SBA's Wiki page. Maximum variable rates are: |
|---|---|
| Loans $50,000 or less | Cannot exceed Prime or SBA Optional Peg Rate + 6.5% |
| Loans $50,001 up to and including $250,000 | Cannot exceed Prime or SBA Optional Peg Rate + 6.0% |

| Product<br>Export Express Loans | Interest Rate<br>The maximum allowable fixed rate is available on SBA's Wiki page. Maximum variable rates are: |
|---|---|
| Loans $250,001 up to and including $350,000 | Cannot exceed Prime or SBA Optional Peg Rate + 4.5% |
| Loans $350,001 and greater | Cannot exceed Prime or SBA Optional Peg Rate + 3.0% |

4. Credit Standards for Export Express

   The policies that make up SBA's credit standards begin with the requirements outlined in 13 CFR §§ 120.101 and 120.150. This section provides procedural guidance as to what the Lender should or must consider when analyzing any request for financial assistance that will be guaranteed by SBA.

   A Lender must analyze each application in a commercially reasonable manner, consistent with prudent lending standards. The cash flow of the Applicant is the primary source of repayment, not any expected recovery from the liquidation of collateral. Thus, if the Lender's financial analysis demonstrates that the Applicant lacks reasonable assurance of repayment in a timely manner from the cash flow of the business, the loan request must be declined, regardless of the collateral available or outside sources of repayment.

   To the maximum extent practicable, Export Express Lenders may use their own forms, internal credit memoranda, notes, collateral documents, and servicing and liquidation documentation. In using their documents and procedures, Lenders must follow their established and proven internal procedures used for their similarly-sized non-SBA guaranteed commercial loans.

   **a. Processing Method**

   Export Express loans are only processed via an Export Express Lender's delegated authority. When a Lender submits an SBA 7(a) loan guaranty request under the Lender's Export Express authority, the Agency does not review the Lender's analysis of the credit or structure of the loan or line of credit prior to issuing a loan number. The Lender must analyze credit worthiness in accordance with SBA Loan Program Requirements and properly document its file. The Export Express Lender's analysis is subject to SBA's review and determination of adequacy, when the Lender requests SBA to purchase its guaranty or when SBA is conducting lender oversight activities.

   **b. Underwriting**

   i. SBA has authorized Export Express Lenders to make the credit decision without prior SBA review. Lenders must not make an Export Express loan that would be available on reasonable commercial terms from either the Lender itself or another source without an SBA guaranty.

ii. The credit analysis must demonstrate there is a reasonable assurance of repayment.

iii. The credit analysis must include the factors demonstrating the Applicant does not have credit available elsewhere on reasonable commercial terms from non-Federal, non-State, non-local government sources, in accordance with Section A, Ch. 1, Para. H, Credit not available elsewhere;

iv. The Lender must use appropriate, prudent, and generally accepted industry credit analysis processes and procedures (which may include credit scoring) and these procedures must be consistent with those used for the Lender's similarly-sized non-SBA guaranteed commercial loans.

v. In addition to using the Lender's appropriate, prudent and generally accepted industry credit analysis and procedures, Export Express Lenders may use a business credit scoring model (such a model cannot rely solely on consumer credit scores) to assess character, reputation, and credit history of the applicant and/or repayment ability if they do so for their similarly-sized, non-SBA guaranteed commercial loans.

a) The business credit scoring model may only be used in addition to the Lender's appropriate, prudent, and generally accepted industry credit analysis and procedures.

b) If used, the business credit scoring results must be documented in each loan file and available for SBA review.

c) Lenders must validate (and document) with appropriate and accepted statistical methodologies that their business credit scoring model is predictive of loan performance and they must provide that documentation to SBA upon request.

d) Although SBLCs do not make non-SBA guaranteed loans, SBA has determined they may use credit scoring. SBLCs are required to provide credit scoring model validation to SBA on an annual basis.

vi. The credit decision on Export Express loans, including how much to factor in a past bankruptcy or whether to require an equity injection, is left to the business judgment of the Lender. Also, if the Lender requires an equity injection and, as part of its standard processes for similarly-sized, non-SBA guaranteed loans verifies the equity injection, it must do so for Export Express loans. While the credit decision is left to the business judgment of the Lender, early loan defaults will be reviewed by SBA pursuant to SOP 50 57. If the application involves a franchise (as defined by FTC), the Lender must review any credit information provided, such as the number of failed franchisees and cash flow projections provided by the franchisor). Lender must review any management agreement (unless the management

agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory) to determine if it results in an ineligible passive company.

vii. Export Express Non-Financial Default Provisions:

Non-financial default provisions are allowed under Export Express under the following conditions:

a) Non-financial default provisions are loan conditions that, if violated, would cause the loan to be in default even though the Borrower has made all payments as agreed.

b) Non-financial default provisions must be substantive and must be agreed to by the Borrower in writing at loan closing;

c) The provisions must be consistent with those used by the Lender on its similarly-sized non-SBA guaranteed commercial loans;

d) A lender may not request purchase of the guaranty solely based on a violation of a non-financial default provision (see 13 CFR § 120.520); and

e) A maturity date must be established in the note. For example, a line of credit could state that it is payable upon demand under certain conditions, but in no case later than a certain date.

**c. Collateral**

See Appendix 19: 7(a) Collateral Requirements Para. B.6

See Section A, Ch. 5, Para. A. for guaranty requirements.

5. Submission of Application for Guaranty for Export Express

See Appendix 20: Submission of Application for Guaranty

## B. EXPORT WORKING CAPITAL PROGRAM (EWCP)

13 CFR § 120.340 - 120.344

Under the EWCP, SBA guarantees short-term working capital loans made by participating lenders to small business Exporters engaged in Export Transactions.

**Lenders must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.**

1. Eligibility for EWCP

   In addition to the Core Requirements identified in Section A, the following EWCP-specific eligibility requirements apply:

   a. Eligibility for EWCP will be limited to businesses that have a history of at least 12 full months of operations prior to filing an application.

      i. In the event that the Applicant or Borrower does not have at least 12 full months of operations, the Lender may perform an analysis that demonstrates sufficient management experience to move forward with the EWCP loan.

   b. The Applicant must be able to produce timely and accurate financial statements, accounts receivable and accounts payable aging, and inventory reports.

   c. Export management companies (EMC) or export trading companies (ETC) may use this program only if the EMC or ETC takes title to the goods or services in the Export Transaction. EMCs or ETCs which have any bank ownership are ineligible for the EWCP loan program.

2. Ineligible NAICS Codes

   For purposes of clarification, small businesses in the following NAICS Industry Subsector Codes cannot be financed using an EWCP loan, but may be financed using other SBA 7(a) financial assistance:

   a. NAICS Industry Subsector Code 721 (Accommodation).

   b. NAICS Industry Subsector Code 457 (Gasoline Stations).

   c. NAICS Industry Subsector Code 722 (Food Services and Drinking Places)

3. Eligible Uses of Proceeds for EWCP

   a. Proceeds can be used only to finance Export Transactions. Loans can be for single or multiple Export Transactions.

      i. Loan proceeds may be used for:

         a) Acquiring inventory for export or to be used to manufacture goods for export, including eligible direct labor and materials;

         b) Paying the manufacturing costs of goods for export;

c) Purchasing goods or services for export;

d) Supporting Performance or Financial standby letters of credit related to export transactions

e) For working capital directly related to export orders

f) For foreign accounts receivable and inventory financing

g) Pre-shipment working capital supporting Export Transactions;

h) Post-shipment foreign accounts receivable financing; and

i) Lender fees and charges and any packaging fees paid as permitted in this Chapter.

j) For refinancing existing short-term export lines of credit with the transfer of collateral in accordance with Appendix 14 Para.A.7.

ii. Loan proceeds may not be used to (13 CFR § 120.342):

a) Support the Borrower's domestic sales;

b) Acquire fixed assets or capital goods for use in the Borrower's business;

c) Provide floor plan financing on titled vehicles or equipment.

d) Finance pre-shipment or purchase order financing under a transaction-specific or transaction-based revolving EWCP facility for Foreign-to-Foreign Export Transactions.

e) Acquire, equip, or rent commercial space overseas; or

f) Finance professional export marketing advice or services, foreign business travel, participation in trade shows or support staff in overseas offices, except to the extent it relates directly to the transaction being financed.

b. Debt Refinancing with Export Working Capital Program (EWCP) Loans: See Appendix 14: 7(a) Debt Refinancing Requirements Para. B.7.

4. Loan Terms and Conditions for EWCP

**a. Maximum Loan Amount**

i. The maximum loan amount is $5,000,000.

ii. Maximum Loans to Businesses with Affiliates

13 CFR § 120.151 Lenders must determine whether the Applicant has any affiliates and document the results in their credit analysis. If affiliation exists, SBA's loan maximums apply to the Applicant, including all affiliates, as if all were a single business.

**b. Maximum Guaranty Amounts and Percentages: See Appendix 16: 7(a) Maximum Guaranty Amounts Para. B.6.**

**c. Loan Maturities: See Appendix 17: 7(a) Loan Maturity Requirements Para. B.7.**

**d. Interest Rates: See Appendix 18: 7(a) Interest Rate Requirements Para. B.7.a.**

**e. Payment Options for EWCP Ongoing Guaranty Fee**

i. For EWCP loans approved after September 27, 2010, the Lender may choose one of the following options for payment of the EWCP Ongoing Fee only. Either option (monthly or annually) will result in payment of the same total amount of EWCP Ongoing Fee on each EWCP loan. Regardless of which payment option is chosen, the Lender must continue to submit, on a monthly basis, the Lender's SBA Form 1502 Report on all 7(a) loans in the Lender's portfolio, including all EWCP loans.

a) Option 1 – Monthly Payment of EWCP Ongoing Fee:
Option 1 allows Lenders to pay the EWCP Ongoing Fee monthly along with other 7(a) loan ongoing servicing fees to the Fiscal Transfer Agent with the required SBA Form 1502 Report. Because EWCP loans may be a small percentage of the Lender's 7(a) portfolio, Option 1 allows Lenders to voluntarily pay the EWCP Ongoing Fee on each EWCP loan on a monthly basis along with the rest of their 7(a) portfolio.

b) Option 2 – Annual Payment of EWCP Ongoing Fee:
Lenders may pay the EWCP Ongoing Fee on each EWCP loan annually by selecting Option 2. Lenders selecting Option 2 will receive an annual invoice on each EWCP loan from SBA's DFC. The EWCP loan balance reported by the Lender on the monthly SBA Form 1502 Reports for the EWCP loan will allow Denver Finance Center (DFC) to compute the EWCP Ongoing Fee amount to be billed annually.

The vast majority of EWCP loans have a maturity of 12 months or less; however, EWCP loans may have a maturity of up to 36 months. For EWCP loans with a maturity of 12 months or less, Lenders will receive one EWCP Ongoing Fee invoice after maturity. For EWCP loans with a maturity in excess of 12 months and not more than 24 months, Lenders will receive an EWCP Ongoing Fee invoice 12 months after closing and again after maturity. For EWCP loans with a maturity greater than 24 months, Lenders will receive an EWCP Ongoing Fee invoice 12 months after closing, 24 months after closing and again after maturity.

The DFC will mail the Lender an EWCP Ongoing Fee invoice on each EWCP loan within 60 days of each 12-month interval on the EWCP

loan and payment will be due within 30 days of the date of the invoice. The invoice will be for the EWCP Ongoing Fee amount owing for the previous 12 months, or shorter period for loans maturing prior to the end of the 12-month period. Lenders will be given instructions on the invoice to make payment using the Pay.gov online payment process.

Fiscal Transfer Agent will send monthly EWCP reports to DFC and SBA's Office of International Trade (OIT). This report will track information on each EWCP loan by Lender, including but not limited to the following:

i) Whether the Lender is submitting SBA Form 1502 Reports on EWCP loans as required;

ii) When annual invoices are to be sent; and

iii) The accrued amount to be billed for the EWCP Ongoing Fee for each EWCP loan.

ii. The DFC will send a monthly report to OIT and SBA's Office of Credit Risk Management reporting any Lenders that are delinquent on payments of invoiced EWCP Ongoing Fees. OIT will be responsible (through delegation to the Export Finance Manager) for monitoring Lenders in regard to submitting the required SBA Form 1502 Reports and the payment of the required EWCP Ongoing Fees. A Lender's failure to pay any of the fees (and any interest and penalties that are subsequently charged by SBA due to a lender's delinquent payment) may result in SBA's decision to suspend or revoke a lender's eligibility to participate in SBA's 7(a) program or to limit a lender's delegated authority.

5. Credit Standards for EWCP

The policies that make up SBA's credit standards begin with the requirements outlined in 13 CFR §§ 120.101 and 120.150. This section provides procedural guidance as to what the Lender should or must consider when analyzing any request for financial assistance that will be guaranteed by SBA.

A Lender must analyze each application in a commercially reasonable manner, consistent with prudent lending standards. EWCP loans are self-liquidating loans, and the conversion of the export-related trading assets to cash is the primary source of repayment. Thus, if the Lender's financial analysis demonstrates that the Applicant lacks reasonable assurance of repayment in a timely manner from the conversion of foreign sales into cash, the loan request must be declined, regardless of the collateral available or outside sources of repayment.

**a. Specific Types of EWCP loans**

i. Transaction-Based Loan: A line of credit that can support a single or multiple

transactions during the term of the loan. A Transaction-Based EWCP may be established on a revolving or non-revolving basis based on the needs of the business.

On no less than an annual basis, the Lender must perform a full review of the credit and collateral securing the EWCP loan in accordance with the requirements in "Annual and Renewal Credit Reviews" in paragraph 6.d below.

ii. Asset-Based Loans (ABLs): ABLs are revolving lines of credit supported by a monthly Borrowing Base Certificate (BBC) that reports levels of assets, typically accounts receivable and inventory, supporting the loan amount. ABLs are typically committed for 12 months and then renewed or re-issued annually.

On no less than an annual basis, the Lender must perform a full review of the credit and collateral securing the EWCP loan in accordance with the requirements in "Annual and Renewal Credit Reviews" in paragraph iv. a) below.

a) Annual and Renewal Credit Reviews.

i) On no less than an annual basis, and as part of any renewal of the loan, the Lender must obtain updated year-end and interim financial statements and perform a full review of the credit and collateral securing the EWCP loan. The Lender's analysis must document that the Applicant:

(a) Is creditworthy.

(b) Has the reasonable assurance of repayment in a timely manner from the conversion of sales into cash; and

(c) Is in compliance with EWCP program requirements.

ii) If the Lender's analysis does not document that all three of the above requirements are met, no further disbursements may be made, and the loan may not be renewed until the Applicant is able to demonstrate that it meets the above three requirements.

**b. Processing Methods**

i. Non-delegated – When a Lender submits an EWCP loan guaranty request under the non-delegated processing method, the Lender submits the application and supporting documents to SBA. SBA will make the final determination as to the eligibility and creditworthiness of the Applicant, including approving the uses of proceeds, the adequacy of the collateral

being pledged, the structure of the loan and any equity injection to be required from the Applicant.

**ii.** Delegated – When a Lender submits an EWCP loan guaranty request under the Lender's PLP-EWCP authority, the Agency does not review the Lender's analysis of the credit or structure of the loan or line of credit prior to issuing a loan number. The Lender must analyze credit worthiness in accordance with SBA Loan Program Requirements and properly document its file. The PLP-EWCP Lender's analysis is subject to SBA's review and determination of adequacy when the Lender requests SBA to purchase its guaranty or when SBA is conducting lender oversight activities.

**c. Underwriting**

Lender must submit a credit memorandum with the application and analyze each EWCP request in a commercially reasonable manner, consistent with prudent lending standards. EWCP loans are self-liquidating loans and the conversion of the export-related trading assets to cash is the primary source of repayment. The Lender's financial analysis should pay particular attention to the Applicant's foreign payment terms and the impact on the Applicant's cash cycle. Lender must specify whether the request is for a single transaction-specific loan, a transaction-based revolving line of credit (single or multiple transactions), or an asset-based loan.

**d. Credit Analysis**

Lender's credit analysis must include the following:

i. An explanation of the use of proceeds and benefits of the loan guaranty, including details of the underlying transaction(s) for which the loan is needed and the country(ies) where the buyer(s) is (are) located;

ii. The factors demonstrating the Applicant does not have credit available elsewhere on reasonable commercial terms from non-Federal, non-State, non-local government sources, in accordance with Section A, Ch. 1, Para. H, Credit not available elsewhere;

iii. A description of the nature of the business, length of time in business under current management and, if applicable, the depth of management experience in the industry or a related industry. Such analysis should include a brief description of the business's management team;

iv. A discussion of the Applicant's export experience and export business plan, which may include the following:

a) Dollar amount of revenues that are or will be generated by export sales, and the percentage of total revenue;

b) Principal or proposed export markets;

c) Proposed or established export customer relationships;

d) Largest export sales contract to date;

e) Export contract backlog discussion; and

f) Documentation of the Applicant's performance history and ability to successfully complete obligations required by standby letter(s) of credit, which serve as bid, advanced payment, performance, supplier, and warranty guarantees and/or bonds.

v. A discussion of financing relationships to include a summary of all short and long term debt relationships, such as:

a) Domestic revolving lines of credit or other term debt credit facilities, which includes a description of the purpose of the debt, payment structure and collateral;

b) Standby debt. Address whether or not the standby debt will permit interest payments to be made and, if so, amounts and frequency, and under what conditions such payments can be halted; and

c) Identify any SBA or other government-guaranteed financing.

vi. A financial analysis of the Applicant's two most recent years of historical financial information (tax returns or balance sheet with debt schedule and income statement) plus an interim statement. The Lender should also provide an analysis of the Applicant's financial projections for at least 12 months after the first disbursement. The analysis shall include:

a) Analysis of historical cash flow and total debt service for the existing business;

b) Calculation of operating cash flow (OCF) defined as earnings before interest, taxes, depreciation, and amortization (EBITDA);

c) Analysis must document additions and subtractions to cash flow such as the following:

i) Unfunded capital expenditures;

ii) Non-recurring income;

iii) Expenses and distributions;

iv) Distributions for S-Corp taxes;

v) Rent payments;

vi) Owner's Draw; and/or

vii) Global cash flow analysis that includes assessment of impact on cash flow to/from any significant affiliate businesses.

vii. Debt service (DS) is defined as the future required principal and/or interest payments on all business debt inclusive of new SBA loan proceeds.

viii. For projected cash flows, the Lender should provide the calculation of debt service coverage using the definitions above, and provide analysis of the assumptions supporting the projected cash flow, such as:

a) Reason for reduced expense structure,

b) Reason for revenue growth, i.e., new product lines, sales channels, and new production facilities; and

c) Industry analysis.

ix. A financial analysis of SBA EWCP loan repayment ability based on the Applicant's cash cycle;

x. Field Examinations.

a) The Lender must perform a field examination prior to the first disbursement on all Asset-Based EWCP loans that are $1,000,000 or greater.

b) Lenders are not required to perform field examinations on Transaction-Based EWCP loans, as each transaction is reviewed individually by the institution.

c) The field examination is an out-of-pocket expense and may be conducted by the Lender's internal audit staff or a third-party examiner. An examination is a verification of the assets that compose the borrowing base. Examinations must include a sampling of the assets (receivables and inventory) included in the borrowing base.

d) If the Asset-Based EWCP loan is $2,000,000 or greater, the Lender must conduct a field examination at least annually.

e) For Asset-Based EWCP loans less than $2,000,000: After the initial field exam prior to the first disbursement (if applicable), the frequency of field examinations may be determined by the Lender based upon the quality of the records, risk profile of the Borrower and seasonality of the line. If the Lender determines that a field examination is not necessary as part of the annual review, the Lender must document the specific circumstances that enabled the decision. Acceptable criteria for not conducting an annual field examination for loans of less than $2,000,000 includes but is not limited to: overall line utilization, level of inventory reliance, suppressed availability, etc.

xi. For Asset-Based loans, a financial analysis of the collateral securing the EWCP loan that addresses any remarks or findings from the field examination.

xii. Ratio calculations for the following financial ratio benchmarks: Current Ratio, Debt/Tangible Net Worth, Debt Service Coverage, inventory turnover, receivables turnover, and payables turnover and any other ratios the Lender considers significant for the business/industry;

xiii. An analysis of the collateral that may include a discussion of:

a) Buyer(s) and export destination market(s) risk, which may include economic, political, compliance, currency, or logistics;

b) Anticipated "terms of sale" on the exports to be financed through the EWCP loan. Terms of sale may include:

i) Cash before Shipment/Cash at Shipment;

ii) Irrevocable Letters of Credit

iii) Export Credit Insurance (for comprehensive commercial and political risk);

iv) Collections (Cash against Documents); and

v) Open Account;

vi) Credit coverage, allowed sales terms, and the Borrower's experience administering the policy.

c) The composition and quality of the collateral in the proposed borrowing base that may include:

i) Quality of the Borrower's customer base;

ii) The presence of concentrations risks;

iii) Delinquency volumes and trends; and

iv) Dilution.

xiv. A discussion of Lender's credit experience with the Applicant and a review of business and personal credit reports.

xv. If the application involves a franchise (as defined by FTC), the Lender must review any credit information provided, such as the number of failed franchisees and cash flow projections provided by the franchisor). Lender must review any management agreement (unless the management agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory) to determine if it results in an ineligible passive company.

**e. Collateral**

See Appendix 19: 7(a) Collateral Requirements Para. B.7.

See Section A, Ch. 5, Para. A. for guaranty requirements.

6. Fees that the Lender May Charge the Borrower

   See Section A., Ch. 4 for requirements for ethics, fees, and Agents.

   In addition to the fees in Section A., Ch. 4, Para. C.2, at the time of the annual review, Lender may charge extraordinary servicing fees in excess of 2% for EWCP loans that are disbursed based on a Borrowing Base Certificate. The fees charged must be reasonable and prudent based on the level of extraordinary effort required and must not be higher than the fees charged on the Lender's similarly-sized, non-SBA guaranteed commercial loans.

7. Submission of Application for Guaranty for EWCP

   See Appendix 20: Submission of Application for Guaranty

## D. INTERNATIONAL TRADE (IT)

13 CFR § 120.345 - 120.349

**Lenders must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.**

1. Eligibility for International Trade Loans

   SBA is authorized to guarantee International Trade Loans to small businesses that are engaged in or preparing to engage in international trade (i.e., in a position to expand existing export markets or develop new export markets) or are adversely affected by import competition to improve the small business's competitive position. In addition to the core requirements identified in Section A, to be eligible for these loans, the Applicant must either 1) be expanding existing or developing new export markets, OR the Applicant 2) be adversely affected by import competition. Within the credit memorandum and the SBA Loan System, the Lender must state which category described in subparagraphs a. and b. below applies to the Applicant. In addition, the SBA Lender must demonstrate how the loan will help the Applicant improve its competitive position, as described in subparagraph c. below.

   a. Development or Expansion of Export Markets:

      The loan proceeds will expand existing export markets or develop new export markets. To establish this, the Applicant must submit an export business plan, including both a projection and narrative rationale that contains enough information to reasonably support the likelihood of expanded export sales.

      i. The plan should identify the amount of expected export sales.

      ii. In such cases, the Applicant must provide documentation to the Lender from the Applicant's domestic customer (typically in the form of a letter, invoice, order, or contract) that the goods or services are in fact being exported.

      iii. For all of the Applicant's exports, the Lender must determine if U.S. companies are authorized to conduct business with the country to which the goods or services will be shipped, pursuant to the Ex-Im Bank Country Limitation Schedule. A loan may not be made to a business that directly or indirectly exports to a foreign country which is listed as a prohibited country (Note #7) on the Country Limitation Schedule without approval from the federal government to export products to those countries; or

   b. Adversely Affected by Import Competition:

      The Applicant must demonstrate injury attributable to increased competition from foreign firms in the relevant market and submit an explanation and financial statements showing that imported products or services which are directly

competitive with those produced or provided by the Applicant have contributed significantly to a decline in competitive position are required. SBA, upon review of U.S. government data, has determined, pursuant to the authority set forth in 15 U.S.C. § 636(a)(16)(D), that small businesses in the following industries meet the threshold eligibility criteria of 15 U.S.C. § 636(a)(16)(D)(i & ii) of having been adversely affected and injured by international trade and increased import competition:

i. Manufacturing NAICS:
   - Sectors 31, 32, 33

ii. Mining, Quarrying, and Oil and Gas Extraction – NAICS:
   - Sector 21
     - Subsectors:
     - 211 – Oil and gas extraction
     - 212 – Mining (Except Oil and Gas)
     - 213 – Support Activities for Mining

iii. Food Supply Chain – NAICS Groups and National Industry Codes:
   - 1111 - Oilseed and Grain Farming
   - 1112 - Vegetable and Melon Farming
   - 1113 - Fruit and Tree Nut Farming
   - 1121 - Cattle Ranching and Farming
   - 1122 - Hog and Pig Farming
   - 1123 - Poultry and Egg Production
   - 1124 - Sheep and Goat Farming
   - 1125 - Aquaculture
   - 1129 - Other Animal Production
   - 1141 - Fishing
   - 1151 - Support Activities for Crop Production
   - 1152 - Support Activities for Animal Production
   - 423820 - Farm and Garden Machinery and Equipment Merchant Wholesalers
   - 4244 – Grocery and Related Product Merchant Wholesalers
   - 4245 – Farm Product Raw Material Merchant Wholesalers

- 424910 – Farm Supplies Merchant Wholesalers
- 445110 – Supermarkets and Other Grocery Retailers
- 484220 –Specialized Freight Trucking, Local – Food Only
- 484230 – Specialized Freight Trucking, Long Distance – Food Only
- 493120 – Refrigerated Warehousing and Storage
- 493130 – Farm Warehousing and Storage

***Note:** NAICS 484220 and 484230 are limited to refrigerated and frozen trucking, farm products, grain products, and livestock.

Loans made to small businesses in the abovementioned industries do not require any additional documentation demonstrating how the Applicant was adversely affected and injured by international trade and increased import competition

c. Improve Competitive Position:

In addition to satisfying the criteria in either paragraph 1.a. or 1.b above, the loan must satisfy the statutory requirement that it will improve the Applicant's competitive position.

To satisfy this requirement, the SBA Lender must document in its credit memorandum how the loan will have a positive impact on the business. This is commonly accomplished by the Lender when summarizing the transaction and reason for the loan request in the credit memorandum.

d. Ineligible Industries:

The following NAICS Industry Subsectors are **ineligible** for International Trade Loans, but may be financed using other SBA 7(a) financial assistance:

i. NAICS Industry Subsector Code 721 (Accommodation)

ii. NAICS Industry Subsector Code 457 (Gasoline Stations).

2. Eligible Uses of Proceeds for International Trade Loans

a. Proceeds of an IT loan may only be used for the following eligible purposes (proceeds of an IT loan may not be used for any other purpose):

i. Acquire, construct, renovate, modernize, improve, or expand facilities and equipment to be used in the United States to produce goods or services;

ii. Working capital (The maximum amount of working capital that can be included in an ITL is $2 million).

iii. Changes of ownership pursuant to the rules outline in Appendix 15: 7(a) Changes of ownership.

a) IT loans approved under the Development or Expansion of Export

Market criteria may be used to support **Business Expansion** and **ESOP & Cooperative** transactions.

b) IT loans approved under the Adversely Affected by Import Competition criteria may be used to support **Business Expansion, Owner Buyout**, and **ESOP & Cooperative** transactions.

c) IT loans cannot be used to support **Initial Acquisition** transactions.

iv. Debt refinancing with an International Trade (IT) loan: See Appendix 14: 7(a) Debt Refinancing Requirements Para. B.8.

3. Loan Terms and Conditions for International Trade

**a. Maximum Loan Amount**

i. The maximum loan amount is $5,000,000.

ii. Maximum Loans to Businesses with Affiliates

13 CFR § 120.151 Lenders must determine whether the Applicant has any affiliates and document the results in their credit analysis. If affiliation exists, SBA's loan maximums apply to the Applicant, including all affiliates, as if all were a single business.

**b. Maximum Guaranty Amounts and Percentages: See Appendix 16: 7(a) Maximum Guaranty Amounts and Percentages Para. B.6.**

**c. Loan Maturities: See Appendix 17: 7(a) Loan Maturity Requirements Para. B.8.**

**d. Interest Rates: See Appendix 18: 7(a) Interest Rate Requirements Para. B.8.**

SBA QUICK REFERENCE CHART: Maximum Interest Rates Allowed

| **Product**<br><br>**International Trade Loans** | **Interest Rate**<br><br>**The maximum allowable fixed rate is available on SBA's Wiki page. Maximum variable rates are:** |
|---|---|
| Loans $50,000 or less | Cannot exceed Prime or SBA Optional Peg Rate + 6.5% |
| Loans $50,001 up to and including $250,000 | Cannot exceed Prime or SBA Optional Peg Rate + 6.0% |
| Loans $250,001 up to and including $350,000 | Cannot exceed Prime or SBA Optional Peg Rate + 4.5% |
| Loans $350,001 and greater | Cannot exceed Prime or SBA Optional Peg Rate + 3.0% |

4. Credit Standards for International Trade

The policies that make up SBA's credit standards begin with the requirements outlined in 13 CFR §§ 120.101 and 120.150. This section provides procedural guidance as to what the Lender should or must consider when analyzing any request for financial assistance that will be guaranteed by SBA.

A Lender must analyze each application in a commercially reasonable manner, consistent with prudent lending standards. The cash flow of the Applicant is the primary source of repayment, not any expected recovery from the liquidation of collateral. Thus, if the Lender's financial analysis demonstrates that the Applicant lacks reasonable assurance of repayment in a timely manner from the cash flow of the business, the loan request must be declined, regardless of the collateral available or outside sources of repayment.

**a. Processing Methods**

i. Non-delegated – When a Lender submits an IT loan guaranty request under the non-delegated processing method, the Lender submits the application and supporting documents to SBA. SBA will make the final determination as to the eligibility and creditworthiness of the Applicant, including approving the uses of proceeds, the adequacy of the collateral being pledged, the structure of the loan and any equity injection to be required from the Applicant.

**ii.** Delegated – When a Lender submits an IT loan guaranty request under the Lender's PLP authority, the Agency does not review the Lender's analysis of the credit or structure of the loan prior to issuing a loan number. The Lender must analyze credit worthiness in accordance with SBA Loan Program Requirements and properly document its file. The PLP Lender's analysis is subject to SBA's review and determination of adequacy, when the Lender requests SBA to purchase its guaranty or when SBA is conducting lender oversight activities.

**b. Underwriting**

i. Lender's Credit Analysis:

The Lender's credit memorandum and analysis must address the Applicant's ability and likelihood to repay the loan from the cash flow of the business and past performance by documenting the following:

a) A description and history of the business, including:

i) Nature of the business, including a description as to how the Applicant meets the specific Loan Program Requirements for an International Trade loan in Paragraph C.1. above;

ii) Length of time in business under current management;

iii) Depth of management experience in the industry or a related industry;

iv) Brief description of the business's management team including principal's involvement in the daily onsite management of the business or how the daily operations will be managed if the principals are not there on a daily basis.

b) Financial analysis of repayment ability:

i) For existing businesses based on the three most recent years of historical financial information (tax returns or balance sheet with debt schedule and income statement) plus an interim financial statement. (13 CFR § 120.191)

ii) For start-ups, new businesses, changes of ownership, and other applications based on projections, include detailed projections, including the supporting assumptions that reflect a debt service coverage equal to or greater than 1.15 within 2 years from loan funding or, for construction projects, within 2 years from the end of construction.

iii) The financial analysis for all Applicants must address the following as applicable:

(a) Historical cash flow for existing businesses that demonstrates total debt service coverage after the SBA loan; if the historical cash flow from the most recent full year and the interim financial statements do not show sufficient debt service coverage, Lender must obtain from the Applicant and analyze 2 years of detailed projections including the supporting assumptions justifying relying on projections instead of historical performance;

(b) Calculation of operating cash flow (OCF) defined as earnings before interest, taxes, depreciation, and amortization (EBITDA);

(c) Justification for additions and subtractions to cash flow such as the following:

(i) Unfunded capital expenditures;

(ii) Non-recurring income;

(iii) Expenses and distributions;

(iv) Distributions for S-Corp taxes;

(v) Rent payments;

(vi) Owner's Draw; and/or

(vii) Global cash flow analysis that includes assessment of impact on cash flow to/from any affiliate business.

(d) The effect any affiliates may have on the ultimate repayment ability of the Applicant.

c) Debt Service (DS) is defined as the future required principal and interest payments on all business debt inclusive of new SBA loan proceeds. The Applicant's debt service coverage ratio (OCF/DS) must be equal to or greater than 1.15 on a historical and/or projected cash flow basis and 1:1 on a global basis. To perform a complete analysis of debt service, it is important for a Lender to obtain a current debt schedule prepared by the Applicant, including any shareholder debt.

d) For cash flow projections, the Lender must calculate the debt service coverage and provide the assumptions supporting the projected cash flow coverage, including as applicable:

i) Justification for revenue growth, i.e., new product lines, sales channels, and new production facilities;

ii) Justification for any reduction in expenses; and

iii) A comparison to current industry trends.

e) Spread of pro-forma Business Balance Sheet (current business balance sheet adjusted for all changes in assets and liabilities as a result of the SBA loan, other debt, any required equity injection and use of loan proceeds);

f) Ratio calculations (based on the pro-forma Balance Sheet and historical and projected Income Statements) for the following financial ratio benchmarks: Current Ratio, Debt/Tangible Net Worth, Debt Service Coverage, and any other ratios the Lender considers significant for the business/ industry (e.g., inventory turnover, receivables turnover, and payables turnover, etc.) including discussion of Lender's comparison to industry trends;

g) Analysis of working capital adequacy, at a minimum over the next 12 months;

h) Assessment of collateral adequacy in accordance with Appendix 19 Para. B.8;

i) Insurance Requirements, including:

i) Life Insurance–- on whom and how much.

ii) Business hazard & liability insurances.

j) Lender must document the refinancing of any debts as part of the loan request, in accordance with the written analysis required in the debt refinancing requirements in Appendix 14. In addition, Lender must

include a written explanation for any late payments over the past 12 months.

k) Lender's rationale for recommending approval, including a discussion and analysis of the following:

i) The factors demonstrating the Applicant does not have credit available elsewhere on reasonable commercial terms from non-Federal, non-State, non-local government sources.

ii) When 50 percent or more of the loan proceeds will be used for working capital, Lender must explain in its credit memorandum why this level of working capital is necessary and appropriate for the subject business;

iii) Competition;

iv) Seller financing;

v) Stand-by agreements;

vi) 90+ day delinquencies;

vii) Trade disputes and/or;

viii) Federal, State, or local citations which would preclude the Applicant from normal business operations;

ix) For a change of ownership, discussion/analysis of the business valuation used to support the purchase price (see Appendix 19 Para. A.1.d. Real estate appraisal and fixed asset valuation requirements);

x) Discussion of any liens, judgments, bankruptcy filings or pending litigation including divorce proceedings; and

l) If the application involves a franchise (as defined by FTC), the Lender must review any credit information provided, such as the number of failed franchisees and cash flow projections provided by the franchisor). Lender must review any management agreement (unless the management agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory) to determine if it results in an ineligible passive company;

ii. Equity requirements (13 CFR § 120.150):

For all loans, depending on whether the loan is processed on a non-delegated or PLP basis, the Lender or SBA must determine that there is sufficient invested equity. To do this, the Lender (for PLP loans) or SBA (for non-delegated loans) must determine if the equity position, any required equity contribution, and the pro forma debt-to-worth are acceptable based on the

factors related to the type of business, experience of management and the level of competition in the market area. The Lender must include a detailed discussion of the equity position (net worth) and any required equity injection. (See Ch. 6, Para. D., Loan Closing and Disbursement, of this Section for requirements concerning documenting and verifying equity injection.)

a) Start-Up Businesses. SBA considers a business to be a "start-up" for the purpose of determining equity injection requirements if it has been in operation (i.e., generating revenue from intended operations) for 1 year or less. SBA considers an equity injection (Applicant contribution) of at least 10 percent of the total project costs (all costs required to become operational, regardless of the source of funds, except for lines of credit and 504 loans) to be necessary for a Start-Up Business to operate on a sound financial basis. All 7(a) loans made to a Start-Up Business require a 10% equity injection based on the project cost; however, loans approved more than 90 days apart from each other are considered to be separate projects.

b) Changes of Ownership: See equity requirements set forth in Appendix 15

c) The following may be considered as equity injection:

i) Standby Agreements - only debt that is on full standby (no payments of principal or interest for the term of the 7(a) loan) may be considered as equity for SBA's purposes. Lender must use SBA Form 155 or its own equivalent Standby Agreement form, and a copy of the note must be attached to the standby agreement. The standby debt may accrue interest and may be added to the standby debt and amortized after the 7(a) loan is paid in full. Standby Creditor must subordinate any lien rights in collateral securing the loan to Lender's rights in the collateral and take no action against Borrower or any collateral securing the Standby Debt without Lender's consent.

ii) Cash that is not borrowed, whether on the business's balance sheet or from other sources.

iii) Cash that comes from a personal loan where repayment can be demonstrated to come from a source other than the cash flow of the business (the salary paid to the owner by the business does not qualify).

iv) Grants that do not have repayment or clawback provisions during the life of the 7(a) loan.

v) Assets other than cash – An appraisal or other valuation by an

independent third party is required if the valuation of the fixed assets is greater than the Net Book Value. A valuation of the fixed assets provided as part of a business valuation will not meet these requirements.

vi) Eligible prepaid expenses that the Lender has verified by obtaining paid invoices, canceled checks, or bank statements. Lender must retain copies of the documentation in the loan file.

(a) Expenses related to education, advisory servicers, or fees paid by the Applicant to an Agent are not eligible prepaid expenses and are not considered equity.

vii) An equity investment not subject to an agreement to repay equity or make distributions to recover an investor's investment prior to release of the guaranty. Note: SBA will considers any investment subject to an agreement to repay equity or make distributions to recover an investor's investment prior to release of the guaranty (e.g., certain types of redeemable preferred stock) to be debt and not equity.

**c. Collateral**

See Appendix 19: 7(a) Collateral Requirements Para. B.8.

See Section A, Ch. 5, Para. A. for guaranty requirements.

5. Submission of Application for Guaranty for International Trade.

See Appendix 20: Submission of Application for Guaranty

# CHAPTER 6: SBA TERMS AND CONDITIONS THROUGH DISBURSEMENT FOR ALL 7(A) LOANS

## A. SBA TERMS AND CONDITIONS

The Lender's executed SBA Form 750 is the written agreement between the SBA and the Lender requiring the Lender to comply with all SBA Loan Program Requirements as defined in 13 CFR § 120.10, including but not limited to, the applicable statute, regulations, and SOP guidance, and allowing the Lender to make loans with an SBA guaranty when authorized by SBA.

The SBA Terms and Conditions is the digital loan guaranty authorization request by the Lender to SBA to authorize the Lender to make the loan with an SBA guaranty under the terms and conditions submitted in the SBA Loan System. SBA's guaranty is subject to the terms and conditions authorized by SBA in the SBA Loan System (including any changes) and the Lender's compliance with those terms and conditions and all other applicable SBA Loan Program Requirements. After the Lender has determined that the loan conditions in the SBA Terms and Conditions are appropriate for the terms of the credit, the Lender must close the loan in accordance with the provisions of the SBA Terms and Conditions, including any SBA-approved post-approval modifications. Unless otherwise required by SBA (e.g., OCRM), the Lender should not send SBA any other loan closing documentation, including disbursement information, except through the required periodic loan status reports using SBA Form 1502. See SOP 50 57 and the Servicing and Liquidation Actions 7(a) Lender Matrix for directions on servicing and liquidating loans. SBA does not require signatures on the terms and conditions. The terms and conditions are electronically stored in the SBA Loan System.

1. For loans processed using a Lender's delegated authority (PLP, PLP-EWCP, SBA Express, or Export Express), the Lender submits the loan guaranty request with the SBA Terms and Conditions. The SBA loan number will be issued in the SBA Loan System.
2. For non-delegated loans processed through LGPC, the Lender submits the loan guaranty request by submitting the loan terms and conditions in the SBA Loan System. SBA will review the application and issue the SBA loan number if the loan is approved.
3. The terms and conditions that must be digitally submitted to the SBA Loan System include:
    a. 7(a) Lender fees payable to SBA:
        i. Statement of the Upfront Fee;
        ii. Statement of Lender's Annual Service Fee;
    b. Repayment terms;
    c. Use of Proceeds;

d. Guarantors;

e. Collateral, including lien priority;

f. Construction terms if applicable in accordance with 4. below.

4. Construction Loan Provisions

13 CFR §§ 120.200 and 120.174

a. In the construction of a new building or an addition to an existing building, regardless of whether the project is one that uses an independent licensed contractor or is a “Do-it-yourself” project, Lender must obtain evidence of compliance with the "National Earthquake Hazards Reduction Program Recommended Provisions for the Development of Seismic Regulations for New Buildings" (NEHRP), or a building code that has substantially equivalent provisions.

i. The NEHRP provisions may be found in the American Society of Civil Engineers (ASCE) Standard 7 and the International Building Code.

ii. Examples of evidence include a certificate issued by a licensed building architect, construction engineer or similar professional, or a letter from a state or local government agency stating that an occupancy permit is required and that the local building codes upon which the permit is based include the Seismic standards.

b. If the construction component of the 7(a) loan is $350,000 or less, SBA has granted a blanket waiver on the Lender’s requirement of a performance bond and the labor and materials payment bond and evidence that the contractor carries appropriate Builder's Risk and Worker's Compensation Insurance when the Lender applies the same policies, procedures, and processes for offsetting the risk of construction that it applies to its similarly-sized, non-SBA guaranteed loans for construction. 13 CFR § 120.200

c. If the construction component of the 7(a) loan is more than $350,000:

Prior to the commencement of any construction, Lender must obtain from Borrower (13 CFR § 120.200):

i. Evidence that the licensed contractor has furnished a l00% performance bond and labor and materials payment bond and that the contractor carries appropriate Builder’s Risk and Worker’s Compensation Insurance;

a) Only a corporate surety approved by the Treasury Department using an American Institute of Architect's form or comparable coverage may issue these bonds.

b) Only Borrower may be named as obligee on the bonds.

c) SBA has granted a blanket waiver on the Lender's requirement of a performance bond and the labor and materials payment bond and evidence that the contractor carries appropriate Builder's Risk and Worker's Compensation Insurance when:

i) The Lender has retained the services of a third party construction management firm. The Lender must ensure that the third party provides commercially reasonable and prudent monitoring including funds control for all disbursements; or

ii) The Lender has an existing internal construction management department that routinely manages construction for its similarly-sized, non-SBA guaranteed commercial loans. The Lender must ensure that the monitoring services provided by its construction management department are commercially reasonable and prudent and include funds control for all disbursements.

iii) Lender must document in the applicable loan file that the construction was completed in conformance with the plans and specifications and that all lien waivers and releases from all material men, contractors, and subcontractors involved in the construction have been obtained. If any mechanics' or other liens are filed or take priority over the Lender's lien on the collateral, the Lender may be subject to a repair or denial of the guaranty. (13 CFR § 120.200)

d) A copy of the final plans and specifications; and

e) A copy of a Construction Contract with:

i) An acceptable licensed contractor at a specified price; and

ii) An agreement that Borrower will not order or permit any material changes in the approved plans and specifications without prior written consent of Lender and the surety providing the required bonds.

ii. Evidence that Borrower has injected the required funds into the project prior to disbursement of the loan, if Borrower is injecting funds into the construction project;

iii. Obtain evidence of Borrower's ability to pay cost overruns or additional construction financing expenses prior to approving any contract modification. Lender and SBA are not obligated to increase the loan to cover cost overruns;

iv. Make interim and final inspections to determine that construction conforms to the plans and specifications;

v. Obtain evidence that the building, when completed, will comply with all state

and local building and zoning codes, and applicable licensing and permit requirements;

vi. Obtain lien waivers or releases from all material men, contractors, and subcontractors involved in the construction.

d. "Do-it-yourself" construction and/or installation of machinery and equipment, or situations where the Borrower acts as its own contractor have proven to be generally unsatisfactory and can cause problems with lien waivers and mechanics liens, causing potential losses to the Lender and/or SBA. "Do-it-yourself" construction including renovations and/or installation of machinery and equipment, or situations where the Borrower acts as its own contractor may be permitted, if the Lender can justify and document in the loan file that:

i. The Borrower/contractor is experienced in the type of construction and has all appropriate licenses;

ii. The cost is the same as, or less than, either:

a) What an unaffiliated contractor would charge as evidenced by 2 bids on the work; or

b) A single estimate provided by a third-party construction management firm, or by the Lender's existing internal construction management department if the Lender has an existing internal construction management department that routinely manages construction for its similarly-sized, non-SBA guaranteed commercial loans.

iii. The Borrower/contractor will not earn a profit on the construction.

## B. POST-APPROVAL MODIFICATIONS

1. Post-approval and prior to final disbursement: See Servicing and Liquidation Actions 7(a) Lender Matrix, and Servicing and Liquidation SOP 50 57, for complete instructions on post-approval modifications. Regardless of processing method (non-delegated or delegated):

a. Lenders must not unilaterally approve any actions that require prior SBA approval. Actions that require prior SBA approval must be submitted to LGPC. The request must include the reason for the action, details of the requested action, supporting documentation, and the Lender's recommendation.

b. Post-approval and prior to final disbursement: Regardless of processing method (non-delegated or delegated), Lenders must inform SBA of certain actions, per the 7(a) Lender Matrix, by making the appropriate change using E-Tran Servicing, or successor SBA Loan System. When the Lender makes the change using E-Tran Servicing, or successor SBA Loan System, a separate notification to the

appropriate SBA center is not necessary (SBA approval of these items is not necessary, and SBA will not respond in writing).

2. For 7(a) loans that have been fully disbursed (**after final disbursement**):
    a. Lenders must submit actions that require SBA notification and requests for prior SBA approval to the CLSC for 7(a) Loans classified in regular servicing status, including partially disbursed revolving lines of credit, which are considered fully disbursed upon initial disbursement.
    b. Lenders must refer to SOP 50 57, 7(a) Loan Servicing and Liquidation, and Servicing and Liquidation Actions 7(a) Lender Matrix to determine if notification or prior approval from SBA is required. All loan increases, regardless of disbursement status, are subject to statutory, administrative, and program maximums and must be approved by SBA. Further, loan increases must be made in accordance with the SOP 50 10 and the Information Notice on 7(a) fees for the fiscal year that were in effect at the time the loan was approved.
3. Loan Increases:
    a. Increases to 7(a) loans, regardless of the disbursement status, are subject to statutory, administrative, and program maximums. Upfront and ongoing fees for increases in subsequent years are at the rates in effect at the time the loan was originally approved. Loan increases must be made in accordance with the SOP 50 10 and the Information Notice on 7(a) fees for the fiscal year that were in effect at the time the loan was approved.
    b. Standard 7(a) (including International Trade), 7(a) Small Loan, EWCP, PLP, PLP-EWCP, SBA Express, and Export Express term loans: If the request for an increase is more than 20% of the original loan amount or is more than18 months after the original approval date of the loan, for loans that were processed under non-delegated procedures, the Lender must request approval from SBA and must include with its request its analysis showing that the purpose of the increase is the same as the original purpose of the loan and that the Borrower's cash flow can support the increased payment amount. For delegated loans, the Lender must document the same analysis and retain it in Lender's loan file.
    c. Revolving lines of credit increases may be made:
        i. If made under SBA Express and Export Express:
            a) At any time during the life of the loan, but must be within 5 years for SBA Express and 7 years for Export Express of the date of loan approval and be in compliance with the maximum maturities on SBA Express and Export Express loans;

b) Must include an analysis of appropriate credit and risk factors consistent with the procedures the Lender uses for its similarly-sized, non-SBA guaranteed commercial loans if the increase is above 33% of the original loan amount.

ii. If made under CAPLines:

a) At any time during the life of the loan, but must be within 10 years of the date of loan approval (except Builder's CAPLines which must be within 5 years of the date of loan approval) and be in compliance with maximum maturities on CAPLines;

b) If the request for an increase is more than 20% of the original loan amount or is more than18 months after the original approval date of the loan, the Lender must include with its request its analysis showing that the purpose of the increase is the same as the original purpose of the loan and that the Borrower's cash flow can support the increased payment amount.

iii. May not exceed the dollar limit for the program at the time the loan was originally approved (this includes any other outstanding loans under SBA Express, Export Express, Community Express and Patriot Express); and

d. SBA Express, and Export Express Increases: Subject to paragraphs 4.a - d. above, Lenders must follow their established and proven internal credit review and analysis procedures used for their similarly-sized, non-SBA guaranteed commercial loans to determine whether the increase is appropriate and must retain all supporting documentation in Lender's loan file. Approval of the requested increase in the SBA Loan System will constitute SBA's prior written consent. SBA may review the documentation supporting the increase when conducting lender oversight activities and at time of guaranty purchase.

## C. TRANSFER OF GUARANTY BETWEEN PARTICIPATING LENDERS

1. To transfer the guaranty between participating Lenders prior to final disbursement, Lender must submit a written explanation to the LGPC along with any supporting documentation. (Transfers after final disbursement must be sent to the CLSC in accordance with SOP 50 57.)

2. To transfer the guaranty on more than one loan prior to final disbursement, Lender must submit a written explanation to the LGPC along with any supporting documentation. The LGPC will forward the request to the D/FA or designee for a decision.

## D. LOAN CLOSING AND DISBURSEMENT

The following instructions for loan closing and disbursement pertain to all 7(a) loans.

Section B, Ch 6: SBA Terms and Conditions through Disbursement for all 7(a) Loans

1. Disbursement Period:

    a. The disbursement period must be stated in the SBA Terms and Conditions. The loan must be fully disbursed within 48 months of approval, or any remaining undisbursed balance will be canceled by SBA. SBA considers a line of credit as fully disbursed at the time of first disbursement. Requests for exceptions to the 48-month disbursement policy: Any requests for an exception to this policy must be submitted in accordance with the "Exceptions to Policy" discussion on page 9 of this SOP and must contain the SBA loan number, a detailed explanation of how cost increases are being financed or, if applicable, explain why there are no cost increases and include any other relevant information. Additionally, the Lender must state how many months the Lender requests to be added to the disbursement period.

    b. Lenders may use an escrow account for not more than 5 business days to facilitate a loan closing. A Lender must not report the loan on SBA Form 1502 as "disbursed" or charge the Borrower the guaranty fee until all funds are disbursed from the escrow account. The Lender may only charge the Borrower interest on funds that have been disbursed out of escrow to the Borrower.

    c. A loan is considered to be fully disbursed and then may be sold on the Secondary Market when the Borrower has access to all of the loan proceeds and is able to use them in accordance with the SBA Terms and Conditions.

2. Note Terms:

    Note terms must include:

    a. All interest rate requirements including, if applicable, any interest-only payment period.

    b. The date of initial adjustment and the frequency of subsequent adjustments;

    c. Maturity date.

    d. Repayment terms:

        i. Lenders using the SBA Note are required to insert the repayment terms from the SBA Terms and Conditions into the Note. The repayment terms may be in any format as long as the information appears in the Note.

        ii. Lenders using their own Note form are required to comply with SBA repayment terms but are not required to use the specific language set forth in the SBA Terms and Conditions.

    e. Loans with a maturity of 15 years or more must contain prepayment/subsidy recoupment fee payable to SBA in accordance with 13 CFR § 120.223.

    f. State-specific language: Lender must ensure that any necessary state-specific

provisions/language is contained in the appropriate loan documents.

g. Repayment terms for CAPLine Loans:

   i. Interest only payments for any period exceeding the Borrower's cash cycle, seasonal cycle, contract final payment date, or project completion date are not permitted.

   ii. Master Notes and Sub-Notes: Each loan will have a Master Note to cover the total loan amount and general repayment period. Lenders can also use a system of sub-notes to establish specific repayment periods for particular seasons, contract, or construction/renovation project. When the CAPLine will be used to finance the creation of more than one asset (such as the completion of two contracts) sub-notes should be used. The conditions of the sub-notes must not conflict with the conditions of the Master Note, except for variances in repayment schedules. See Paragraph D.4, Required SBA Forms, below.

h. Escrow Policy for Commercial Real Estate Taxes and Insurance:

   i. The Borrower and Lender may agree to establish an escrow account for the purpose of collecting and paying real estate taxes, hazard insurance, and/or flood and earthquake insurance, when applicable;

   ii. The amount of money collected for an escrow account may not exceed 105% of the amount charged in the current year by the taxing authority or insurance company for the total requirement to pay the annual real estate taxes and insurance;

   iii. The account must be FDIC-insured and pay the Borrower a money market rate of interest, or the rate typically paid on escrow accounts for commercial real property on non-SBA guaranteed loans, whichever is greater;

   iv. Except for those items covered in subparagraphs h. ii and iii immediately above, the account must be consistent with accounts required of the Lender's conventional Borrowers and the Lender must use similar procedures to administer the escrow accounts on its SBA loans as it does for its non-SBA guaranteed loans (SBLCs must be consistent with the practices followed by federally-regulated Financial Institutions);

   v. Lender must remit to the Borrower all accrued interest on the account and provide annual statements, unless otherwise required by state or Federal law; and

   vi. Upon termination of the account, the remaining funds must be returned to the Borrower within 15 business days.

i. For loans being sold on the secondary market, in addition to the above:

Section B, Ch 6: SBA Terms and Conditions through Disbursement for all 7(a) Loans

i. The date the complete loan application is received by SBA. This is the date the loan is approved and assigned an SBA loan number.

ii. Initial interest rate as percent.

iii. If Note interest rate fluctuates, full description of Base Rate, e.g., Prime Rate; Alternative Base Rate, e.g., SOFR; publication source, e.g., WSJ; spread over Base Rate as a percent; date of first fluctuation as either an exact date or a description of date, e.g., first calendar quarter following first disbursement; change period, e.g., calendar quarterly.

iv. If applicable, interest rate ceiling and floor.

v. Maturity as exact date or description of date, e.g., 300 months from date of Note.

vi. First payment due date as either an exact date or a description, e.g., one month from date of Note.

vii. Payment frequency, e.g., monthly

viii. Payment due date, e.g., 14th of the month

ix. Payment amount

x. With regards to Borrower payment application: Lender will apply each installment payment first to pay interest accrued to the day Lender receives the payment, then to bring principal current, then to pay any late fees, and will apply any remaining balance to reduce principal.

xi. Language covering prepayment:

Notwithstanding any provision in this Note to the contrary, Borrower may prepay this Note. Borrower may prepay 20% or less of the unpaid principal balance at any time without notice. If Borrower prepays more than 20% and the Loan has been sold on the secondary market, Borrower must:

a) Give Lender written notice;

b) Pay all accrued interest; and

c) If the prepayment is received less than 21 days from the date Lender receives the notice, pay an amount equal to 21 days' interest from the date lender receives the notice, less any interest accrued during the 21 days and paid under b., above. If Borrower does not prepay within 30 days from the date Lender receives the notice, Borrower must give Lender a new notice.

xii. Subsidy Recoupment Fee language, if applicable:

When in any one of the first three years following the date of first disbursement Borrower voluntarily prepays more than 25% of the outstanding principal balance of the loan, Borrower must pay to lender on behalf of SBA a prepayment fee for that year as follows:

a) During the first year after the date of first disbursement, 5% of the total prepayment amount;

b) During the second year after the date of first disbursement, 3% of the total prepayment amount;

c) During the third year after the date of first disbursement, 1% of the total prepayment amount.

3. Closing Documentation:

a. For all 7(a) loans, Lender must disburse the loan proceeds in accordance with the SBA Terms and Conditions.

b. All Lenders must document each disbursement on an SBA-guaranteed loan. Except under SBA Express, Export Express, and 7(a) Small Loans, Lender and Borrower must use and complete and sign SBA Form 1050 or Lender's equivalent form at the time of first disbursement. If there are subsequent disbursements, Lender must document each disbursement and attach the documentation to the original SBA Form 1050. The documentation must contain sufficient detail for SBA to determine:

i. The recipient of each disbursement;

ii. The date and amount of each disbursement; and

iii. The purpose of each disbursement.

c. The Lender must obtain evidence to support disbursements, such as cancelled checks or paid receipts, to ensure that the Borrower used loan proceeds for purposes stated in the SBA Terms and Conditions. If the SBA Terms and Conditions identifies working capital as a use of proceeds and those proceeds will be used to pay normal operating expenses (e.g., payroll, utilities, etc.), then the working capital disbursement does not need to be documented.

d. The following documentation is acceptable to verify disbursement in accordance with the SBA Terms and Conditions:

i. Joint payee checks;

ii. Copies of receipts, invoices or other supporting documentation marked paid by the seller or vendor; or

iii. Evidence of an electronic funds transfer to a vendor along with a copy of the invoice.

e. The Lender must retain in its loan file the signed SBA Form 1050 as well as all supporting documents.

f. Documentation of Equity Injection:

i. With the exception of SBA Express and Export Express loans, Lenders must verify the SBA-required equity injection prior to disbursing any loan proceeds and must maintain evidence of such verification in their loan files. Lenders are expected to use reasonable and prudent efforts to verify that equity is injected and used as intended, and failure to do so may warrant a repair or partial/full denial. Lenders must submit this documentation with each purchase request on a loan for which SBA requires an equity injection. Verifying a cash injection requires the following documentation:

a) A copy of a check or wire transfer along with evidence that the check or wire was processed showing the funds were moved into the Borrower's account or escrow;

b) A copy of the most recent statement(s) (covering at least 30 days) from the account where the funds are being withdrawn (showing that funds were available); and

c) A statement from the Borrower's account documenting the funds were deposited or a copy of a settlement statement or HUD-1 showing the use of the cash.

ii. A promissory note, "gift letter," or financial statement is not sufficient evidence of cash injection without corroborating evidence consistent with Subparagraph f. i. immediately above.

iii. If the equity injection will come from any form of borrowed funds, such as a HELOC or seller financing in excess of the minimum Borrower injection requirements outlined above, Lender must address the proposed repayment terms as well as any Standby or Subordination terms that will be in place.

iv. For SBA Express and Export Express loans, if a Lender requires an equity injection and, as part of its standard processes for similarly-sized, non-SBA guaranteed commercial loans verifies the equity injection, it must do so for its SBA Express and Export Express loans.

4. Required SBA Forms:

a. For all 7(a) loans, Lenders have the option of using their own Note and guaranty agreements or the SBA versions (SBA Forms 147, 148 and 148L).

i. If the Lender uses its own Note form, the Lender must ensure that the Note is legally enforceable and assignable, has a stated maturity and is not payable

on demand. In addition, regardless of delivery method, when the Lender uses its own Note form, the Note **must** include the following language:

"When SBA is the holder, this Note will be interpreted and enforced under Federal law, including SBA regulations. Lender or SBA may use state or local procedures for filing papers, recording documents, giving notice, foreclosing liens, and other purposes. By using such procedures, SBA does not waive any Federal immunity from state or local control, penalty, tax, or liability. As to this Note, Borrower may not claim or assert against SBA any local or state law to deny any obligation, defeat any claim of SBA, or preempt Federal law."

ii. Lenders that intend to sell the loan guarantee into the SBA Secondary Market are strongly encouraged to use the SBA Form 147. If a Lender uses its own form of a note, all terms and conditions in the SBA Form 147 must be included in the document. The Fiscal Transfer Agent reviews notes other than the SBA Form 147 to ensure that all required terms and conditions for sale are satisfied, which may increase processing time for loan sales settlement.

iii. Regardless of the delivery method, when the Lender uses its own guaranty form (Lender's equivalent of SBA Form 148/148L), the guaranty **must** include the following language:

"When SBA is the holder, the Note and this Guarantee will be interpreted and enforced under Federal law, including SBA regulations. Lender or SBA may use state or local procedures for filing papers, recording documents, giving notice, foreclosing liens, and other purposes. By using such procedures, SBA does not waive any Federal immunity from state or local control, penalty, tax, or liability. As to this Guarantee, Guarantor may not claim or assert any local or state law against SBA to deny any obligation, defeat any claims of SBA, or preempt Federal law."

b. The following language must appear in all lien instruments, including mortgages, deeds of trust, and security agreements:

"The Loan secured by this lien was made under a United States Small Business Administration (SBA) nationwide program which uses tax dollars to assist small business owners. If the United States is seeking to enforce this document, then under SBA regulations:

i. When SBA is the holder of the Note, this document and all documents evidencing or securing this Loan will be construed in accordance with Federal law.

ii. Lender or SBA may use local or state procedures for purposes such as filing papers, recording documents, giving notice, foreclosing liens, and other

purposes. By using these procedures, SBA does not waive any Federal immunity from local or state control, penalty, tax, or liability. No Borrower or Guarantor may claim or assert against SBA any local or state law to deny any obligation of Borrower or defeat any claim of SBA with respect to this Loan.

iii. Any clause in this document requiring arbitration is not enforceable when SBA is the holder of the Note secured by this instrument."

c. Any documentation the lender uses for its similarly-sized, non-SBA commercial loans.

d. Fee Disclosure and Compensation Agreement, SBA Form 159, for Lender fees in excess of $2,500.

e. Fee Disclosure and Compensation Agreement, SBA Form 159 for any Agents.

f. Equal Employment Opportunity Poster, SBA Form 722 (for all loans).

g. IRS Form 4506-C, IVES Request for Transcript of Tax Return or IRS Form 8821, Tax Information Authorization, in accordance with Section A, Ch. 5, Para. B, IRS Tax Transcript/Verification of Financial Information.

5. Collateral:

The Lender must obtain all required collateral and must meet all other required terms and conditions as applicable before or at the time of disbursement. Required terms and conditions include requirements identified in the credit memorandum, such as cash/equity injections, standby agreements, appraisals or evaluations, etc.

Lenders must obtain a valid and enforceable security interest in any loan collateral with evidence of proper lien priority and must retain in their loan file proof of the lien filings, and, when received, proof of the recordation of the liens.

Lenders may sell loans on the secondary market after filing a required lien with the appropriate office, but before receiving proof from the appropriate office that the required filing was recorded, However, if the loan defaults, and there is a loss resulting from the Lender's failure to obtain a properly perfected and recorded required lien with the required priority, the Lender will be subject to a full or partial denial of liability equal to the guaranteed share of the net loss.

6. Licenses:

The Lender must obtain evidence from the Borrower of all licenses required to operate the business within no more than 90 days after final disbursement of the loan. The loan may not be sold into the secondary market until all required licenses are obtained.

7. Required Lender Action:

In accordance with the Debt Collection Improvement Act of 1996, Lenders are required to report information to the appropriate credit reporting agencies whenever they extend credit via an SBA loan. Thereafter, the Lender should continue to routinely report information concerning servicing, liquidation, and charge off activities throughout the life cycle of the loan, as specified in SOP 50 57 or a successor procedural guide.

8. Borrower Certifications:

    a. Lender must obtain certain certifications and agreements from the Borrower(s) (OC and EPC) prior to disbursement of loan proceeds. Borrower and OC must certify that:

        i. They received a copy of the SBA Terms and Conditions or the Lender's equivalent;

        ii. There has been no adverse change in Borrower's (and OC's) financial condition, organization, operations, or fixed assets since the date the Loan Application was signed;

        iii. No principal who holds at least 50 percent of the ownership or voting interest of the Borrower or OC is delinquent more than 60 days under the terms of any administrative order; court order; or repayment agreement requiring payment of child support;

        iv. Borrower and OC are current on all federal, state, and local taxes, including but not limited to income taxes, payroll taxes, real estate taxes and sales taxes; and

        v. If applicable, the Borrower(s) and the 401(k) plan are in compliance with all applicable IRS, Treasury, and Department of Labor requirements and will comply with all relevant operating and reporting requirements.

        vi. Environmental - For any real estate pledged as collateral for the loan or where the Borrower or OC is conducting business operations, the Borrower or OC are in compliance with all local, state, and Federal environmental laws and regulations and will continue to comply with these laws and regulations. Furthermore, they are unaware of any other actual or potential environmental hazards related to the collateral or business premises. They agree to fully indemnify Lender and SBA against all liabilities or losses arising from the contamination of the property before or during the term of the loan.

        vii. The Borrower and/or OC will reimburse Lender for out of pocket expenses incurred in the making and administration of the loan;

        viii. The Borrower and/or OC will maintain proper books and records, allow Lender and SBA access to these records, and furnish financial statements or reports annually or whenever requested by Lender;

ix. The Borrower and/ or OC will post SBA Form 722, Equal Opportunity Poster, where it is clearly visible to employees, applicants for employment and the general public;

x. To the extent practicable, they will purchase only American-made equipment and products with the proceeds of the loan;

xi. They will pay all Federal, state, and local taxes, including income, payroll, real estate, and sales taxes of the business when they come due;

xii. For debt refinance, the debt being refinanced was used exclusively for the Applicant's business, including any credit card, HELOC, and/or debt on the balance sheet; and

xiii. During the life of the loan, the real estate if purchased by proceeds of the 7(a) loan pledged as collateral for the loan or where the Borrower or Operating Company conducts its business operations will not be leased to or occupied by any business that Borrower or Operating Company knows is engaged in any activity that is illegal under Federal, state or local law or any activity that can reasonably be determined to support, promote, or facilitate any activity that is illegal under Federal, state, or local law.

b. Borrower and OC must certify that they will not, without the Lender's prior written consent:

i. Make any distribution of company assets that will adversely affect the financial condition of the Borrower and/or OC;

ii. Change the ownership structure or interests in the business during the term of the loan; or

iii. Sell, lease, pledge, encumber (except by purchase money liens on property acquired after the date of the Note), or otherwise dispose of any of the Borrower's property or assets, except in the ordinary course of business.

9. Separate Loan Agreement:

SBA does not require a separate loan agreement to be signed by the Borrower. If the Lender requires a separate loan agreement on its non-SBA guaranteed loans, it must do so on its SBA-guaranteed loans. The Lender may use its own form of loan agreement.

10. PLP Program:

a. SBA closing requirements are the same for loans guaranteed through delegated PLP processing as for non-delegated loans. The same forms are required.

b. The Lender should not send SBA any other closing documentation, including disbursement information, except through the required periodic loan status reports using SBA Form 1502 or as specifically requested by SBA (e.g., OCRM).

11. SBA Express, Export Express, and 7(a) Small Loans:

    a. A Lender must use the same written closing and disbursement procedures and documentation as it uses for its similarly-sized non-SBA guaranteed commercial loans in addition to meeting the requirements of Paragraph D.4., Required SBA Forms above. There must be a promissory note that is legally enforceable and assignable in the event that it would ever have to be assigned to SBA.

    b. The Lender must obtain all required collateral and must meet all other required conditions before loan disbursement, including obtaining valid and enforceable security interests in any loan collateral. These conditions include requirements identified in the loan write-up, such as standby agreements, appraisals or evaluations, business licenses, and cash/equity injections.

    c. Before disbursing an SBA Express, Export Express or 7(a) Small Loan, the Lender must:

        i. Verify Borrower financial information in accordance with Section A, Ch. 5, Para. B, IRS Tax Transcript/Verification of Financial Information.

        ii. Obtain evidence of no un-remedied adverse change since the date of the application (or since any of the preceding disbursements in the case of multiple disbursements), in the financial or any other condition of the Borrower that would warrant withholding any disbursement. For revolving line of credit disbursements, Lenders should essentially follow the same practices as they do for their non-SBA guaranteed commercial revolving lines of credit.

        iii. Obtain, where applicable, required hazard insurance.

        iv. Make, where applicable, the required flood hazard determination and require flood insurance, if applicable.

        v. In the construction of a new building or an addition to a building, obtain the Borrower's agreement that the construction will conform to the "National Earthquake Hazards Reduction Program Recommended Provisions for the Development of Seismic Regulations for New Buildings".

        vi. Obtain the Borrower’s agreement that it will, to the extent feasible, purchase only American-made equipment and products with the proceeds of the loan. This certification is included on the SBA Form 1919.

        vii. Obtain the Borrower’s certification that no principal who holds at least 50 percent of the ownership or voting interest of the Borrower or OC is delinquent more than 60 days under the terms of any administrative order; court order; or repayment agreement requiring payment of child support.

        viii. Require, where applicable, appropriate environmental reviews and

compliance in Section A, Ch. 5, Para. E, Environmental Policies and Procedures. Lenders may not request a loan number for a loan that will be secured by collateral that will not meet SBA's environmental requirements or that will require use of a non-standard indemnification agreement.

d. Regardless of processing method or size of loan: Within 15 business days after final disbursement, the Lender must submit to SBA through E-Tran Servicing, or successor SBA Loan System, any changes to the terms and conditions that were in place at the time the SBA loan number was issued and retain all other documents in the Lender's loan file.

e. Access to Funds: Loan funds may be accessed through a variety of methods consistent with the way the Lender normally conducts business for its similarly-sized, non-SBA guaranteed commercial loans. Use of a credit or debit card to access the loan funds is acceptable. In providing access through credit or debit cards, Lenders must ensure that these loans are documented by legally enforceable and assignable promissory notes.

## SECTION C. 504 LOAN PROGRAM SPECIFIC REQUIREMENTS

This section, along with Section A, Core Requirements for all 7(a) and 504 Loans, contains the policies and procedures governing SBA's 504 Loan Program.

### CDCs must always start by reviewing the contents of Section A, Core Requirements for all 7(a) and 504 Loans.

SBA recognizes the importance of giving special consideration to veterans in its loan programs. SBA will prioritize processing applications from businesses that are owned by veterans when those loans are processed by SBA under non-delegated procedures. For loans processed under delegated procedures, SBA encourages CDCs and Third Party Lenders to give special consideration to veterans during application processing.

# CHAPTER 1: ELIGIBILITY THROUGH SUBMISSION OF APPLICATION

**Purpose of the 504 Loan Program**

The 504 loan program is an economic development program to create and preserve job opportunities and stimulate growth, expansion, and modernization of small businesses. This program can be used to finance fixed assets for eligible small businesses. 13 CFR § 120.2(c)

## A. PRIMARY PROGRAM ELIGIBILITY FACTORS

A 504 Project must achieve at least one of the following Economic Development Objectives: 13 CFR §§ 120.860, 120.861, and 120.862

3. Job Creation or Retention (Dollars per Job) requirements as follows:
    a. A Project must create or retain one job opportunity per $95,000 guaranteed by SBA except that, in the case of a Project of a Small Manufacturer (defined as a small business with its primary NAICS Code in Sectors 31, 32, and 33 with all its production facilities located in the United States) or a project that meets an Energy Public Policy Goal, the Project must create or retain one job opportunity per $150,000 guaranteed by SBA.
    b. For Projects that are eligible under 13 CFR 120.862, "Other economic development objectives," a CDC's portfolio must reflect an average of one job opportunity for every $150,000 guaranteed by SBA; and
    c. For Projects in Alaska, Hawaii, state-designated enterprise zones, empowerment zones, and enterprise communities, labor surplus areas (as determined by the Secretary of Labor), and for other areas designated by SBA (which include Opportunity Zones), the CDC's portfolio may average not more than $150,000 per job created or retained.

2. Other Economic Development Objectives and Public Policy Goals

    A Project that achieves one of the Community Development or Public Policy Goals listed in 13 CFR § 120.862 is eligible if the CDC's portfolio of 504 loans, including the subject loan, meets or exceeds the CDC's required job opportunity average as described in Paragraph b. below. Loan applications must indicate how the Project will meet the specified economic development objective. 13 CFR § 120.862

    a. Additional guidance for the Energy Public Policy Goals authorized by 13 CFR § 120.862(b)(11-13):

        **Energy Public Policy Projects**: Projects meeting the requirements in **i., ii., or iii. below** are Energy Public Policy Projects.

The Energy Public Policy Projects described in subparagraphs i. and ii. below are eligible for the loan amounts described in Paragraph D.1., Debenture Limits, below (hereafter referred to as "Eligible Energy Public Policy Projects").

Note: The terms in subparagraphs ii. and iii. below have the meanings given those terms under the Leadership in Energy and Environmental Design (LEED) standards for green building certifications. For additional information on LEED Certification, see https://new.usgbc.org/leed.

i. Projects for the reduction of existing energy consumption by at least 10%. This category may not be used for Projects involving new businesses. In addition, if this project involves:

   a) The construction or acquisition of a facility:

      i) The new facility must replace an existing facility.

      ii) The energy consumption at the existing facility must be compared with the new facility, and the Applicant must be able to demonstrate that the new facility will use 10% less energy than the existing facility. The energy consumption between the two facilities must be compared for energy consumption on a square footage basis.

      iii) The new facility must be located in the same local area (e.g., the same city, town, county, zip code, metropolitan statistical area or as otherwise deemed appropriate by SBA).

   b) The retrofit of an Applicant's existing facility, the retrofit must reduce the energy consumption of that facility by at least 10%, regardless of the energy usage of any other facilities that the Applicant may operate; or

ii. Renewable energy sources that generate more than 15% of energy used at Project Facility.

   a) This category includes plant, equipment, and process upgrades of renewable energy sources such as the small-scale production of energy for individual buildings or communities' consumption, commonly known as micropower, or renewable fuel producers including biodiesel and ethanol producers.

   b) Each Project must generate more than 15% of the energy used by the Applicant at the Project facility. In addition, all improvements or equipment required to generate the renewable energy or renewable fuels must be included in the 504 Project costs; **or**

iii. Increased use of sustainable designs. Increased use of sustainable designs, including designs that reduce the use of greenhouse gas emitting fossil fuels

or low-impact design to produce buildings that reduce the use of non-renewable resources and minimize environmental impact.

iv. With respect to paragraphs i. and ii. above, the Applicant must document the Energy Public Policy Project's compliance through either an energy audit, engineering report, or other professional evaluation, as deemed appropriate by SBA, that is based on the annual energy usage at the facility or facilities (measured in actual energy usage, e.g. kilowatt hours, therms, or gallons, as applicable, not in dollar costs), and that, at a minimum, includes the following:

a) A description of the facility or facilities;

b) The current energy usage;

c) The projected energy usage, which must be based on all modifications and retrofits to building(s), and all installations of, and replacements and retrofits to, equipment; and

d) The qualifications of the party performing the energy audit, engineering report, or other professional evaluation, each of which must be performed by an independent third party (by an entity other than the Applicant, the interim lender, the Third Party Lender, or any of their respective affiliates).

b. A CDC's portfolio must maintain a job opportunity average of one Job Opportunity created or retained for every:

i. $95,000 guaranteed by SBA; or

ii. $150,000 guaranteed by SBA for Projects located in Special Geographic Areas (Alaska, Hawaii, State-designated enterprise zones, empowerment zones, enterprise communities, Opportunity Zones[1], and labor surplus areas) A CDC may choose to separate these loans from the remainder of its portfolio for the purpose of calculating the averages.

iii. Loans to Small Manufacturers and eligible Energy Public Policy Projects are excluded from this average.

3. If the 504 Project cannot satisfy any of these Economic Development Objectives and guidelines described above, then the amount of the debenture must be reduced to meet the job creation or retention requirement.

[1] An "Opportunity Zone" is an economically distressed community that has been nominated by the State and certified by the Secretary of the U.S. Treasury as a community in which new investments, under certain conditions, may be eligible for preferential tax treatment. More information and a list of Opportunity Zones for all States are available at https://www.cdfifund.gov/Opportunity-Zones.

## B. THIRD PARTY LENDER PARTICIPATION

| Typical 504 Structures | | | |
|---|---|---|---|
| | Standard Financing Structure | New Business OR Limited or Special Purpose Property | Both New AND Limited or Special Purpose Property |
| Third Party | 50 | 50 | 50 |
| CDC/SBA | 40 | 35 | 30 |
| Borrower | 10 | 15 | 20 |

A 504 project has three main partners and generally: a Third Party Lender provides 50% or more of the financing; a Certified Development Company (CDC) provides up to 40% of the financing through a 504 debenture (guaranteed 100% by SBA); and an applicant (Borrower) injects at least 10% of the financing (13 CFR §§ 120.801 and 120.900). No more than 50% of eligible Project costs can be from Federal sources (13 CFR § 120.930(a)).

1. **Third Party Loan** 13 CFR § 120.920

    a. The Third Party Lender must be in place at the time of application and must be evidenced by a letter of intent/term sheet or commitment letter included in the application package outlining the terms and conditions of the Interim and/or Third Party Loan to enable SBA to evaluate the 504 application.

    b. For any 504 project with total project costs of at least $5,000,000, the CDC must obtain and retain the Third Party Lender's underwriting analysis and incorporate that analysis into the CDC credit memorandum. The Third Party Lender may submit their entire credit memorandum to the CDC or only the narrative and financial analysis, omitting sections on additional products and services or risk ratings.

    The CDC's credit memorandum must, at a minimum, summarize the TPL's assessment of repayment ability, collateral coverage, and material loan terms, and must identify any differences between the TPL's analysis and the CDC's conclusions.

    c. The maturity of the Third Party Loan may not exceed that of the debenture term. Additional terms of the Third Party Loan are defined in 13 CFR § 120.921.

    d. The Third Party Loan must be at least as much as the net debenture proceeds. However, the Third Party Loan must total at least 50% of the Project costs if the Borrower (or Operating Company if the Borrower is an Eligible Passive Company) has operated for 2 years or less or the Project is for the acquisition, construction, conversion or expansion of a limited or single purpose asset.

    e. The Third Party Loan may be closed and begin amortizing prior to the debenture funding.

f. The Third Party Lender's note and loan documents must not have any cross-default, "deem-at-risk," or any other provisions which allow the Third Party Lender to make demand prior to maturity unless the loan is in default.

g. The 504 loan is usually collateralized by a second lien on Project Property. The Third Party Lender may obtain additional collateral or other security for the Third Party Loan in addition to its lien on the Project Property ("Additional Collateral") only if in the event of liquidation and unless otherwise approved in writing by the D/OFPO:

   i. The Third Party Lender liquidates or otherwise exhausts all reasonable avenues of collection with respect to the Additional Collateral no later than the disposition of the Project Property, and

   ii. The Third Party Lender applies any proceeds received as a result of the Additional Collateral to the balance outstanding on the Third Party Loan prior to the application of proceeds from the disposition of the Project Property to the Third Party Loan.

h. Interest Rate Swap Contracts:

   i. An interest rate swap is a contract between two parties where one party pays a fee in exchange for an agreement by the other party to pay any interest in excess of an established amount. The contract may last for all or part of the term of the loan. The swap contract only relates to the payment of interest.

      Example: A Borrower has a prime plus 2% interest rate on a Third Party Loan variable rate loan (presently 5.25%). The Borrower could purchase an interest rate swap contract that would set the interest rate at 7%. When the Note rate is lower than the rate paid by the Borrower on the swap contract (7%), the swap seller keeps the extra amount as compensation for the risk that rates will at some point exceed 7%. When the Note rate is higher than the rate paid by the Borrower on the swap contract, the Borrower would continue to pay the fixed rate of 7% and the swap seller would pay the difference above 7% to the lender. The ability to stabilize the amount of the loan payment each month is the benefit to the Borrower of an interest rate swap contract.

   ii. Third Party Loans may use swap contracts. In order to use an interest rate swap on a Third Party Loan, the interest rate swap contract must meet the following conditions:

      a) The interest rate swap contract is an agreement between the small business Borrower and the lender or, if the swap seller is not the lender, a third party. SBA is not a party to the interest rate swap contract.

b) SBA will not review swap contracts for Borrowers or provide guidance on their use. While swap contracts should not have a significant impact on the cost of the loan, SBA will not publish any guidelines on the cost of these contracts.

c) Swap contracts may be used on new or existing Third Party Loans.

d) The swap contract does not have to last for the entire length of the Third Party Loan.

e) SBA does not have a standard form for an interest rate swap contract.

f) Any fees owed the swap counterparty as a result of the default by the Borrower will be subordinated to the SBA 504 loan.

i. CDCs must not enter into any Intercreditor agreement with the Third Party Lender other than SBA Form 2287, "Third Party Lender Agreement," without the prior written consent of SBA.

2. Interim Financing

Loans under the 504 program provide permanent or take-out financing (see Ch. 2, Para. C.2. Escrow Closing, below in this Section, for the requirements of an escrow closing with no interim loan). An interim lender (either the Third Party Lender or another lender) provides the interim financing to cover the period between SBA approval of the project and the debenture sale. After the project is completed, the CDC will close the 504 loan. The proceeds from the Debenture sale repay the interim lender for the amount of the 504 project costs that it advanced on an interim basis.

a. Any experienced, independent source including the Third Party Lender may supply interim financing provided they meet the conditions described in 13 CFR § 120.890. A CDC may provide interim financing but only for a project financed by another CDC. As stated in the regulation, neither the Borrower nor an Associate of the Borrower may supply interim financing.

b. If the Third Party Lender provides the interim loan, it may do so using:

i. An interim note which will be paid in full with the net debenture proceeds and a permanent note; or

ii. A single note, which includes both the interim and permanent financing that will be reduced by the net debenture proceeds.

3. Financing Involving Industrial Development Bonds or Industrial Revenue Bonds

SBA may participate in Projects financed in part, directly or indirectly, by obligations exempt from state or local taxes (for example, real estate tax exemptions). However, in accordance with OMB Circular A-129, "Policies for Federal Credit Programs and Non-Tax Receivables" (January 2013), *SBA may not participate in projects financed in part, directly or indirectly, by Federal tax-exempt obligations.* For Projects that do not involve

Federal tax-exempt obligations, industrial development bonds or industrial revenue bonds (IDBs/IRBs) may be a source of funding for Projects under the following conditions:

a. When the bond proceeds are used to fund the Third Party Loan:

   i. If the bond issuer requires that it hold title to the Project Property, the TPL's and SBA's respective liens must be properly recorded before any transfer of the title to the Project Property to the bond issuer;

   ii. If the bond issuer takes title to the Project Property and leases the Project Property to the Borrower, the bond issuer must assign the lease to the Third Party Lender and all payments under the lease must be paid to the Third Party Lender and serve as the payments under the loan;

   iii. If subparagraphs a. i. and a. ii. are met, then the Third Party Loan may remain in a senior lien position.

   iv. If the bond issuer does not require that it hold title to the Project Property but takes a lien on the Project Property, the Third Party Lender may still be in a senior lien position, but SBA's lien position must not be subordinate to the bond issuer's lien.

b. When the bond proceeds are used to fund the Borrower's Contribution:

   i. If the bond issuer requires that it hold title to the Project Property, the TPL's and SBA's respective liens must be properly recorded before any transfer of the title to the Project Property to the bond issuer;

   ii. SBA's lien position must not be subordinate to the bond issuer's lien; and

   iii. The Borrower may not pay the loan made from the proceeds of the tax-exempt obligation at a faster rate than the 504 loan unless it is approved by the D/FA or designee;

c. In no case may a default in payment of the tax-exempt obligation result in a tax lien on the property; and

d. In transactions where the bond issuer takes collateral other than the Project Property, SBA may, in its discretion, agree to take a subordinate lien position on that collateral.

   The structure of these transactions may vary from state to state and other conditions may apply.

4. Financing Involving Historic Rehabilitation Tax Credits

Under IRS regulations (Internal Revenue Code § 50), the owner of property eligible for historic rehabilitation tax credits may lease the property, and transfer the historic rehabilitation tax credits, to another party (the "Tax Credit Investor"). SBA may participate in Projects involving such tax credits under the following conditions:

a. In such situations where the Borrower is the owner of the property eligible for the historic rehabilitation tax credits, the Project Property may be leased by the Borrower to the Tax Credit Investor and then must be simultaneously subleased back from the Tax Credit Investor to the Borrower. The term of the sublease must be equal to the term of the lease.

b. The transfer of the rehabilitation tax credits from the Borrower to the Tax Credit Investor must comply with all applicable IRS requirements.

c. Copies of the lease and the sublease that will be executed by the Borrower and the Tax Credit Investor must be submitted with the 504 application. The executed copies of both leases must be submitted for review (including legal review by SBA counsel) prior to closing. This review will be limited to ensuring that the terms of the two leases are equal.

   SBA's lien on the Project Property must not be subordinate to the lease between the Borrower and the Tax Credit Investor.

d. The loan may not be structured as an EPC/OC loan.

e. The structure of these transactions may vary case-by-case, and CDCs and the SLPC should consult with SBA Counsel and OCA for additional guidance. SBA may also participate in projects where the Borrower transfers State rehabilitation tax credits if such projects satisfy all applicable State requirements and the other requirements set forth above.

## C. ELIGIBLE USES OF PROCEEDS

13 CFR §§ 120.882 - 120.884

CDCs must always start by reviewing the contents of Section A, **Core Requirements for all 7(a) and 504 Loans**.

1. Land and Necessary Land Improvements

   (For example, grading, new streets including curbs and gutters, parking lots, utilities, and landscaping.) No matter how long the land has been owned, the value of the land:

   a. Will be based on cost only if it was purchased less than 2 years prior to the date of the application; and

   b. Will be based on the fair market value of the land as determined by an independent real estate appraisal that meets the requirements in Paragraph E.2.b, Appraisals, below if the land has been held for 2 years or more;

   c. May include the costs of building and building improvements such as facade expenditures, heating, electrical, plumbing and roofing costs.

   d. The value of the land also may include the costs of solar panels and associated equipment and installation costs unless:

i. The primary purpose of the solar panels is to produce electricity for sale (i.e., solar farms), in which case the panels are treated as machinery and equipment; or

ii. The solar panels are part of a system that is leased to the Borrower and owned by a third party, and ownership of these assets will not transfer to the Borrower at the end of the lease.

2. Machinery and Equipment

   a. All costs associated with the purchase, transportation, dismantling or installation of machinery and equipment;

   b. The machinery and equipment must have a useful life of at least 10 years;

   c. If the Borrower owns equipment that is heavy or highly calibrated (such as a large printing press) that must be moved as an essential part of the Project, then any special moving costs (including dismantling and installation) may be included in the project costs.

3. Furniture and Fixtures

   If essential to and a minor part of the Project which will not affect the weighted average maturity;

4. Professional Fees

   If directly attributable and essential to the Project with the exception of attorney's fees incurred in closing the Interim and Third Party Loans. Examples of project-related costs that may be included in this section are title insurance; title searches and abstract costs; surveys; and zoning matters;

5. Other Applicant Expenditures

   For any of the costs listed in subparagraphs 1 through 4 above incurred by the Applicant (with its own funds or from a Short-Term Debt) prior to the date of application that are directly attributable to the Project, provided such expenditures (net of Applicant's contribution) are reimbursed by the Interim Lender;

6. Short-Term Debt

   Short-Term Debt (aka "Bridge Financing") the purpose of which was to provide financing until longer term financing could be obtained for any of the costs listed in subparagraphs 1 through 5 above that are directly attributable to the Project, provided that the financing is for a term of 3 years or less;

7. Interim Financing

   Repayment of interim financing including points, fees, and interest;

8. Contingency Fund

May not exceed 15% of the Project construction costs:

a. If the residual contingency amount does not exceed 2% of the debenture just prior to closing, it may be refunded to the small business as working capital at the time the debenture is funded.

**b.** If the contingency residual is in excess of 2% of the debenture just prior to closing, the funds may not be distributed to the small business as working capital, and the debenture must be reduced by the unused amount.

9. "Do-it-yourself" Construction

"Do-it-yourself" construction, including renovations, and/or installation of machinery and equipment, or situations where the Applicant acts as its own contractor have proven to be generally unsatisfactory and can cause problems with lien waivers and mechanics liens, causing potential losses to lenders and/or SBA.

"Do-it-yourself" construction, including renovations, (e.g., installation of carpeting or painting) and/or installation of machinery and equipment may be permitted, if the CDC can justify and document in the loan file that:

a. The Borrower/contractor is experienced in the type of construction and has all appropriate licenses;

b. The cost is the same as, or less than, either:

i. What an unaffiliated contractor would charge as evidenced by two bids on the work; or

ii. A single estimate provided by a third-party construction management firm, or by the Third-Party Lender's existing internal construction management department if the Third-Party Lender has an existing internal construction management department that routinely manages construction for its similarly-sized non-SBA guaranteed commercial loans.

c. The Borrower/contractor will not earn a profit on the construction.

10. Permissible Debt Refinance without Expansion

13 CFR § 120.882(g)

SBA may approve a Refinancing Project of a Qualified Debt that does not involve an expansion as follows.

a. Definitions

i. "Qualified Debt" means a commercial loan that:

a) Either:

i) Substantially all (75% or more) of the proceeds of the existing debt was used to acquire an Eligible Fixed Asset(s) and the remaining

amount (25% or less) was incurred for the benefit of the small business seeking refinancing; or

ii) If the Eligible Fixed Asset(s) was originally financed through a commercial loan (hereafter the "original loan") that was subsequently refinanced one or more times:

(a) Substantially all (75% or more) of the proceeds of the original loan was used to acquire an Eligible Fixed Asset(s) and the remaining amount (25% or less) was incurred for the benefit of the small business seeking the refinancing; and

(b) The existing debt is the most recent refinancing of the original loan.

b) Was fully disbursed not less than 6 months prior to the date of application.

c) Was incurred for the benefit of the small business that is seeking the refinancing.

d) Has been secured by Eligible Fixed Asset(s) for at least 6 months.

e) May include debt subject to a federal guarantee under these conditions:

i) An existing 504 loan if both the Third Party Loan and the 504 loan are being refinanced or the Third Party Loan has been paid in full, and

ii) The CDC has notified the existing CDC or 7(a) Lender in writing by letter or email no less than 10 business days to advise them the existing loan is being refinanced. The notification must be included in the loan submission.

iii) The refinancing of a Federally-guaranteed loan provided a substantial benefit to the borrower after Eligible Business Expenses, prepayment penalties, financing fees, and other financing costs are accounted for. "Substantial benefit" will mean that the portion of the new installment amount attributable to the debt being refinanced must be less than the existing installment amount(s). In calculating the percentage reduction in the new installment payment, prepayment penalties, financing fees, and other financing costs, must be added to the amount being refinanced, but not Eligible Business Expenses. The CDC may request the D/FA or designee to approve an exception to the reduction requirement for good cause. PCLP CDCs may not use their delegated authority to approve a loan requiring this exception.

iv) If the loan being refinanced is guaranteed by a Federal agency other than SBA, the CDC must document in writing that the refinancing of

the Federally-guaranteed loan is permissible under the other Federal agency's requirements or is otherwise approved by the other Federal agency.

f) If the CDC can demonstrate that the commercial real estate provides adequate collateral protection for the SBA, any liens on machinery and equipment purchased with proceeds of the original loan can be waived. A TPL or lender may require additional collateral not required by SBA for the 504 project property.

g) Is not a Third Party Loan which is part of an existing 504 Project, except as provided in Paragraph 10.a.i.e)i) above; and

h) May consist of a combination of two or more loans, provided that each of the loans satisfies the Qualified Debt requirements.

ii. "Eligible Fixed Assets" are one or more long-term fixed assets, such as land, buildings, machinery, and equipment, acquired, constructed, or improved by a small business for use in its business operations.

iii. "Refinancing Project" means the fair market value of the Eligible Fixed Asset(s) securing the Qualified Debt and any other fixed assets acceptable to SBA (Additional fixed assets may be added only when needed to comply with the 90% Loan-to-Value Limitation described in C.10.i below). A refinancing project may include funds for Eligible Business Expenses.

iv. "Eligible Business Expenses (EBE)" are payments of the business for either Operating Expenses or Other Secured Debt that:

a) Are limited to the "Operating Expenses" which are expenses of the business that were incurred but not paid prior to the date of the 504 application or that will become due for payment within 18 months after the date of application. Examples include salaries, rent, utilities, inventory, and other expenses of the business that are not capital expenditures.

b) Business Lines of credit and business credit cards may be included, if:

i) Loan proceeds are not used to cover any personal expenses;

ii) If the line of credit and/or credit card was used for personal expenses, the Applicant must identify which purchases were for personal expenses and deduct that amount from the amount to be refinanced as an EBE;

iii) The line of credit and/or credit card are in the name of the small business; and

iv) The Applicant and the CDC certify in the loan application that the debt

being refinanced was incurred exclusively for EBE.

c) "Other Secured Debt" is debt incurred prior to the 504 loan application that has been secured by the same Eligible Fixed Assets securing the Qualified Debt and incurred for the benefit of the Borrower and/or Operating Company. Other Secured Debt does not include debt incurred for the purposes of capital expenditures, and any existing liens must be released or subordinated to the amount of the debt being refinanced by the 504 loan.

i) This debt must be secured for at least 6 months prior to the date of application by the same Eligible Fixed Asset(s) securing the Qualified Debt; and

ii) The Borrower has been current on all payments due for not less than 12 months preceding the date of application. "Current on all payments due" means that no payment was more than 30 days past due from either the original payment terms or modified payment terms (including deferments) if such modification was agreed to in writing by the Borrower and the lender of the existing debt note less than one year prior to the date of application.

d) If the Borrower is requesting that the refinancing include EBE, the application must include a specific description and an itemization of the amount of each expense.

e) The CDC must retain in its file the following EBE documentation:

i) EBE must be itemized (a gross figure is not acceptable).

ii) The CDC's credit memorandum must:

(a) Document the nature of the EBE;

(b) Provide the itemization of EBE; and

(c) Include the CDC's certification that the EBE are eligible as defined in this Paragraph.

b. The Applicant must have been in operation for all of the 2-year period ending on the date that the application is submitted, as evidenced by the financial statements submitted at the time of application. If the business has been in operation for more than 2 years at the time of application, and there has been a change of ownership in the business, the CDC must determine, under the standards contained in the definition of New Business in Appendix 3, whether the Applicant should be considered a New Business and the application declined. The CDC must document the justification for its determination in its credit memorandum.

c. The Refinancing Project must include Qualified Debt, as defined below. In

addition, the Refinancing Project may include Eligible Business Expenses, as defined below. The amount of the Refinancing Project is also subject to the Loan-to-Value Limitations in Paragraph C.10.i below.

d. In accordance with 13 CFR § 120.882(g)(5), the funding for the Refinancing Project must come from three sources based on the current fair market value of the fixed assets serving as collateral for the Refinancing Project, including an amount from the Third Party Lender that is at least as much as the 504 loan (Net Debenture proceeds), not more than 40% from the 504 loan, and not less than either a 10% or 15% contribution from the Borrower as determined under 13 CFR § 120.882(g)(5).

e. If the Qualified Debt is not fully satisfied by the funding provided by the Refinancing Project, the lender of the Qualified Debt must take one of the following actions, or some combination thereof, to address the deficiency;

   i. Forgiveness of all or part of the deficiency;

   ii. Acceptance of payment by the Borrower; or

   iii. Acceptance of a Note executed by the Borrower for the balance, or any portion of the balance. Such Note must be subordinate to the 504 loan if the Note and the 504 loan are secured by any of the same collateral. The Note is subject to any other restrictions that SBA may establish to protect its creditor position, including standby requirements.

f. If the Qualified Debt (including the original loan as defined in Paragraph C.10.a.i.a)ii) above) was for the construction of a new building, or the acquisition, renovation, or reconstruction of an existing building, and such loan would not have satisfied the leasing policies set forth in 13 CFR §§ 120.131 and 120.870(b), Borrower must be able to demonstrate compliance with 13 CFR § 120.131(b) for existing buildings as of the date of application for assistance.

g. When the Refinancing Project involves a Limited or Special Purpose Property (see the Limited or Special Purpose Property List at Paragraph E.1.c.i.c) below), the Borrower must comply with the Borrower contribution requirements in Paragraph E.1.c, below.

h. Notwithstanding 13 CFR § 120.860, a debt may be refinanced under this Paragraph 10 if the Refinancing Project does not meet the job creation or other economic development objectives set forth in 13 CFR § 120.861 or 13 CFR § 120.862. In such case, the 504 loan may not exceed the product obtained by multiplying the number of employees of the Borrower by $95,000. The number of employees of the Borrower is equal to the sum of:

   i. The number of full-time employees of the Borrower on the date of the application, and

ii. The product obtained by multiplying:

a) The number of part-time employees of the Borrower on the date of the application; by

b) The quotient obtained by dividing the average number of hours each part time employee of the Borrower works each week by 40.

Example: 30 full-time employees and 35 part-time employees working 20 hours per week is calculated as follows: 30 + (35 x (20/40)) = 47.5. The maximum amount of the 504 loan would be 47.5 multiplied by $95,000, or $4,512,500.

i. Loan-to-Value Limitations

i. For projects that refinance only Qualified Debt, the maximum loan to value of the Refinancing Project allowed is 90%.

ii. For projects when the amount of Qualified Debt being refinanced is more than 90 percent of the value of the Eligible Fixed Asset(s) securing the Qualified Debt, the Borrower must provide additional cash or other fixed asset collateral acceptable to SBA so as not to exceed a 90% loan to value of the Refinancing Project.

iii. For any projects that include the financing of Eligible Business Expenses, a maximum 90% loan to value of the Refinancing Project will apply. The value of the Refinancing Project may not be increased by adding additional collateral.

j. Fees

i. In addition to the annual guarantee fee assessed under 13 CFR § 120.971(d)(2), Borrower must pay SBA a supplemental annual guarantee fee to cover any additional cost attributable to the refinancing in an amount established by SBA each fiscal year. The CDC should follow the instructions in the SBA Terms and Conditions to ensure the fee is correct.

ii. SBA will review the fee annually to determine whether it needs to be changed and, if so, will issue a notice of any change.

k. Other Implementation Guidelines

i. Borrower must meet all current 504 Loan Program occupancy requirements at time of application.

ii. PCLP CDCs may not approve, under their delegated authority, the refinancing of an existing loan of the PCLP CDC, or its affiliates (i.e., Same Institution Debt) and must submit the 504 loan to SBA for approval. This requirement is consistent with SBA's long-standing policy of prohibiting its participating lenders from using their delegated authority to approve the

financing of same institution debt due to the potential conflict of interest and the risk of the 504 loan proceeds being used to shift to SBA a potential loss from the existing debt.

iii. Loans for Debt Refinance without Expansion must be disbursed within 9 months after loan approval. The D/FA or designee may approve a request for extension of the disbursement period for an additional 6 months for good cause.

l. Documentation Requirements

i. Credit memorandum. The CDC must provide an analysis in its credit memorandum that the proposed debt refinancing satisfies each of the requirements of this debt refinancing program, including the requirements described in paragraphs 10.a.i.a) through h), 10.a.iv. a) through e), 10.b., 10.d., 10.e., 10.f., and 10.i. above.

ii. In its commitment letter (Exhibit 14 of SBA Form 1244), the Third Party Lender must certify that it has no reason to believe that the following statements in paragraphs a) and b) below are not true:

a) Either:

i) Substantially all (75% or more) of the proceeds of the indebtedness being refinanced were used to acquire an Eligible Fixed Asset (e.g., land, including a building situated thereon, to construct a building thereon, or to purchase equipment) and the remaining amount (25% or less) was incurred for the benefit of the small business seeking the refinancing; or

ii) If the Eligible Fixed Asset(s) was originally financed through a commercial loan (the “original loan”) that was subsequently refinanced one or more times:

(a) Substantially all (75% or more) of the proceeds of the original loan was used to acquire an Eligible Fixed Asset (e.g., land, including a building situated thereon, to construct a building thereon, or to purchase equipment) and the remaining (25% or less) was incurred for benefit of the small business seeking the refinancing; and

(b) The existing debt is the most recent refinancing of the original loan.

b) All of the proceeds of the indebtedness being refinanced were used for the benefit of the small business.

c) In addition, if the indebtedness being refinanced is debt of the Third Party Lender, or any of its affiliates (Same Institution Debt), the Third

Party Lender must certify in its commitment letter that it is not in a position to sustain a loss on the Refinancing Project causing a shift to SBA of all or part of a potential loss from the existing debt.

iii. Transcripts. The CDC must obtain a copy of the current transcript of account, or equivalent, for the Qualified Debt being refinanced and submit and/or retain it as required by SBA Form 1244. See Exhibit 19 of SBA Form 1244. The CDC must determine whether the loan to be refinanced involves a creditor that is in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from an existing debt and document the justification for its determination in the credit memorandum. It is prohibited for a 504 Loan to be used to pay any creditor in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from an existing debt under 13 CFR § 120.884(b).

iv. Appraisal. Appraisals are not required at time of application. Appraisals dated within 12 months of the date the application was approved are required prior to closing, and appraisals must otherwise comply with the requirements for appraisals in Paragraph E.2.b, below.

v. Documentation to Verify Lien(s) at Application. In considering the Borrower's application, the CDC must obtain evidence that lien(s) are securing the Qualified Debt with Eligible Fixed Asset(s), and state in its credit memorandum that it has verified that the lien(s) has been in place for at least 6 months prior to the date of application. The CDC must retain the evidence of the liens in its records (e.g., Preliminary Title Report, Mortgage Deed of Trust, or UCC-1 filing).

vi. Interim Lender Documentation. The Interim Lender must execute SBA Form 2288R, Interim Lender Certification for Refinancing Program, similar to what is required in all 504 closings.

m. Same Institution Debt

i. When the loan being refinanced is Same Institution Debt (as defined in 13 CFR § 120.882(g)(16)), and the loan is not part of an existing 504 Project and is held 100% by the lender that will be the Third Party Lender of the Refinancing Project, the Third Party Lender may modify its existing loan documents (Note, Deed of Trust/Mortgage, etc.) instead of requiring the Borrower to execute and record new loan documents for the Third Party Loan.

ii. All modified loan documents must meet SBA's regulatory requirements for a Third Party Loan (see 13 CFR §§ 120.920 and 120.921).

iii. When the loan being refinanced is Same Institution Debt, either an Interim Loan or an escrow account may be used, and:

a) The Third Party Lender (who, in this case, is also the Lender of the debt being refinanced) must execute SBA Form 2416, "Lender Certification for Refinanced Loan."

b) The CDC may create an escrow account ("account") at the time of closing of the 504 loan for the purpose of holding the Borrower's cash contribution, if any, and the net debenture proceeds.

c) The account will be established in accordance with an Escrow Agreement, which must be executed by the Borrower, the Third Party Lender, the Escrow Agent, and the CDC. The account may be held by the CDC attorney or Title Company or other party approved by SBA.

d) The Borrower's cash contribution, if any, must be deposited into the account at the time of closing of the 504 loan.

e) A copy of the Escrow Agreement must be provided to SBA with evidence of funding by Borrower's cash contribution, if any, at the time of closing of the 504 loan.

f) The net debenture proceeds must be wired to the account, and all funds may be released only upon written approval by the CDC and SBA, provided that CDC/SBA have the required lien positions on the collateral as set forth in the SBA Terms and Conditions and Debenture Guaranty.

g) The debt to be refinanced will be satisfied by payment of the escrowed funds to the Third Party Lender.

n. A 504 Project cannot be approved to refinance debt owed:

i. To an Associate, which is prohibited by 13 CFR § 120.130(a);

ii. To an SBIC or a New Markets Venture Capital Company (NMVCC), which is prohibited by 13 CFR § 120.130(b); or

iii. To any creditor in a position to sustain a loss causing a shift to SBA of all or a part of a potential loss from an existing debt. 13 CFR § 120.884(b).

11. Permissible Debt Refinancing with Expansion

13 CFR § 120.882(e)

504 Projects may include a limited amount of debt refinancing with expansion, as follows.

a. If the Project involves expansion of an Applicant, any amount of existing indebtedness that does not exceed 100% of the cost of the expansion may be refinanced. The debt being refinanced will be added to the expansion cost to establish the total project costs, if all the conditions discussed below are met. A

"Project involves Expansion" if it involves the acquisition, construction, or improvement of land, building or equipment for use by the Applicant.

b. The CDC must provide an analysis in its credit memorandum that the proposed debt refinancing satisfies each of the requirements below:

   i. Either:

      a) Substantially all (75% or more) of the proceeds of the existing debt was used to acquire a fixed asset(s) that was eligible for financing under the 504 loan program and the remaining amount (25% or less) was incurred for the benefit of the small business seeking refinancing; or

      b) If the fixed asset(s) was originally financed through a commercial loan (hereafter the "original loan") that was subsequently refinanced one or more times:

         i) Substantially all (75% or more) of the proceeds of the original loan was used to acquire the fixed asset(s) and the remaining amount (25% or less) was incurred for the benefit of the small business seeking the refinancing; and

         ii) The existing debt is the most recent refinancing of the original loan.

   ii. The existing indebtedness is collateralized by fixed assets.

   iii. The 504 eligible fixed assets collateralizing any debt to be refinanced or relating to the portion of debt being refinanced in the case of a partial refinance, must also collateralize the 504 Loan unless SBA (SLPC) approves a waiver due to extraordinary circumstances. PCLP CDCs may not use their delegated authority to approve a loan requiring this waiver. The lender of the existing indebtedness must release, subordinate (if the total existing indebtedness is not being refinanced) or assign its lien on the 504 eligible fixed assets to the lien of SBA and/or the Third Party Lender so that the Third Party Lender and/or SBA will maintain the same lien position on the collateral that was held by the lender whose debt is being refinanced.

   iv. The existing indebtedness was incurred for the benefit of the small business concern.

      a) The small business for which the debt is being refinanced must be the same small business for which any new Project costs are incurred. The debts being refinanced may be owed by an Operating Company, an Eligible Passive Company or both.

      b) An existing 504 loan may be refinanced if it meets the conditions of this Paragraph and either: both the Third Party Loan and the 504 loan are being refinanced; or the Third Party Loan has been paid in full and the

504 loan needs to be refinanced as part of a larger transaction to provide funding for expansion or renovations to the Project Property. In either case, the CDC and Third Party Lender must document its loan file as to the justification to refinance the existing SBA-guaranteed 504 loan. Any applicable 504 prepayment penalties will apply. A Third Party Loan may not be refinanced with an SBA-guaranteed loan. (13 CFR § 120.920(b))

c) An existing 7(a) loan may be refinanced in whole or in part. A 504 loan may only be refinanced in whole. The CDC must notify an existing 7(a) or 504 Lender in writing by letter or email no less than 10 business days to advise them the existing loan is being refinanced.

v. The financing will be used only for refinancing existing indebtedness or costs relating to the Project financed.

a) Debt being refinanced does not need to be for assets at the same location or for the same type of property as the Project being financed as long as the operation at the other location has the same NAICS code as the operation at the Project location.

b) Costs essential to the refinancing, such as prepayment penalties, financing fees or other refinancing costs, required by the original terms of the debt instrument, may be included in the debt refinance portion of a Project.

c) The total debt being refinanced may consist of one or more loans.

vi. The financing will provide a substantial benefit to the Borrower when prepayment penalties, financing fees, and other financing costs are accounted for.

"Substantial Benefit" means that the portion of the new installment amounts attributable to the debt being refinanced must be less than the existing installment amount(s). The total installment amount is determined by adding the two installment amounts attributable to the refinancing using the interest rate of the most recent debenture funding on the 504 loan and the committed interest rate of the Third Party Lender loan. The total amount must be less than the existing installment amount(s).

a) Prepayment penalties, financing fees, and other financing costs must also be added to the amount being refinanced in calculating the reduction in the new installment payment.

b) Loans with seasonal payments would meet the Substantial Benefit test if there was an improvement in the installment when calculated by averaging all payments over the most recent twelve month period from

date of application and comparing that to the new installment amount attributable to the debt being refinanced.

c) Loans with balloon payments meet the Substantial Benefit test independent of the reduction requirement.

vii. The Borrower has been current on all payments due on the existing debt for not less than 1 year preceding the date of refinancing. "Date of refinancing" refers to the date the 504 loan is approved by SBA. The CDC must submit a transcript of account, or similar documentation containing detailed payment history from the lender whose debt is being refinanced reflecting that the loan has been current (not to exceed 30 days in arrears) for 1 year (or for the time the debt has been open if less than 1 year). Any unremedied delinquency after approval must be reported to SBA as an adverse change.

viii. The financing under section 504 will provide better terms or rate of interest than the existing indebtedness on the date of refinancing. "Better terms or rate of interest" may include longer maturity (but always commensurate with the assets' useful life), a lower interest rate committed on the Third Party Lender Loan or projected on the 504 Loan, improved collateral conditions, or less restrictive loan covenants.

c. PCLP authority must not be used to refinance Same Institution Debt. "Same Institution Debt" is defined as any debt of the CDC or the Third Party Lender financing the new project, or of affiliates of either. 13 CFR § 120.882(e)(8)

d. Whether the new project is within the CDC's area of operation is based on the assets newly acquired for the business and not on the assets securing the debt being refinanced. If the assets refinanced or any collateral securing the loan are outside the CDC's Area of Operations, it is the CDC's responsibility to establish that the CDC is capable of closing and servicing the loan and monitoring the collateral. Evidence must be approved by SBA with the exception of PCLP CDCs, which must document the file with evidence regarding the CDC's capability to close and service the loan and monitor the collateral.

e. Instruments resulting in transfer of ownership of the property to the Applicant may be eligible for refinancing, including, but not limited to, land sales contracts, contracts for deed or capital leases.

f. The purchase of property under an operating lease is eligible for 504 financing, but the operating lease itself is not eligible for debt refinancing.

g. In order to be eligible for debt refinancing, a copy of the corresponding debt and lien instruments must be submitted with the application.

h. Equity in land and/or building that is being refinanced may be included as Borrower's equity as set forth under present policy.

i. In its commitment letter (Exhibit 14 of SBA Form 1244), the Third Party Lender must certify that it has no reason to believe that the following statements in paragraphs i. and ii. below are not true:

i. Either:

a) Substantially all (75% or more) of the proceeds of the indebtedness being refinanced were used to acquire an Eligible Fixed Asset (e.g., land, including a building situated thereon, to construct a building thereon, or to purchase equipment) and the remaining amount (25% or less) was incurred for the benefit of the small business seeking the refinancing; or

b) If the Eligible Fixed Asset(s) was originally financed through a commercial loan (the "original loan") that was subsequently refinanced one or more times:

i) Substantially all (75% or more) of the proceeds of the original loan was used to acquire an Eligible Fixed Asset (e.g., land, including a building situated thereon, to construct a building thereon, or to purchase equipment) and the remaining (25% or less) was incurred for benefit of the small business seeking the refinancing; and

ii)The existing debt is the most recent refinancing of the original loan.

ii. All of the proceeds of the indebtedness being refinanced were used for the benefit of the small business.

iii. In addition, if the indebtedness being refinanced is debt of the Third Party Lender, or any of its affiliates (Same Institution Debt), the Third Party Lender must certify in its commitment letter that it is not in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from the existing debt.

j. A 504 Project cannot be approved to refinance debt owed:

i. To an Associate, which is prohibited by 13 CFR § 120.130(a);

ii. To an SBIC or a New Markets Venture Capital Company (NMVCC), which is prohibited by 13 CFR § 120.130(b); or

iii. To any creditor in a position to sustain a loss causing a shift to SBA of all or a part of a potential loss from an existing debt. 13 CFR § 120.884(b)

12. Eligible Administrative Costs

The administrative costs set out in 13 CFR § 120.883 are not part of the Project costs but are added to the Net Debenture to calculate the Gross Debenture amount. For more information on fees, see Section A, Ch. 4, Para. E, 504 Loan Program Fees and Use of Agents. Examples of Borrower's out-of-pocket costs include:

a. Settlement agent's fees;

b. Overnight delivery, postage, and messenger services;

c. Certifications required by SBA (such as earthquake, flood, IRS, Certificate of Occupancy, and certificate of completion); and

d. Copying costs attributable to the above.

13. Change of Ownership

a. Projects that result in a change of ownership are eligible under the following circumstances:

i. The 504 Project finances only the costs associated with eligible long-term fixed assets; the acquisition of any other assets such as receivables or goodwill is not an eligible use of 504 loan proceeds or Third Party Loan proceeds and must be financed by other means, which may include a 7(a) loan;

ii. The application documents that jobs will be created or retained because of the change of ownership. The application must demonstrate that there is a reasonable basis upon which to conclude that the retained jobs would be lost without the change of ownership. This can be in the form of a statement from the seller to that effect with supporting facts or other certification acceptable to the SLPC.

iii. Loan proceeds may be used to finance a change of ownership between existing owners in an existing EPC when the asset(s) of the EPC are limited to real estate and/or other eligible long-term fixed assets that the EPC leases to one or more Operating Companies ("OC") for conducting the OC's business and when the change of ownership will result in the purchasing owner(s) owning 100% of the EPC. SBA recognizes that an EPC's balance sheet may include limited assets in addition to the real estate or other eligible long-term fixed assets, such as capital replacement reserves or escrow accounts for taxes and/or insurance (such assets are ineligible assets). In such case, 504 loan proceeds may be used to finance a change of ownership between existing owners of the EPC as long as:

a) The ineligible assets are directly related to the real estate or other eligible long-term fixed assets;

b) The amount attributable to such ineligible assets is de minimis; and

c) The ineligible assets are excluded from the Project financing.

See Section A, Ch. 2, Para. A, Eligible Passive Companies for more information on EPC/OC requirements.

b. The 504 loan proceeds must not be used to purchase stock or any other ownership interest in a business unless, by purchasing the stock or other ownership interest, the Applicant is purchasing the real estate where the Applicant is located and/or other eligible long-term fixed assets used in the Applicant's business operation. To the extent the value of the stock or other ownership interest exceeds the value of the real estate and/or other eligible long-term fixed assets ("excess value"):

   i. The excess value cannot be financed by the Project financing; it must be financed separately; and

   ii. The excess value must be de minimis compared to the value of the real estate and/or other eligible long-term fixed asset(s).

c. The change of ownership must result in the Applicant owning 100% of the business.

d. The seller may not remain as an officer, director, stockholder or Key Employee of the business.

e. All other 504 Loan Program Requirements must be met.

14. Pre-Existing Debt on the Project Property

    13 CFR § 120.922

    In addition to its share of Project cost, a Third Party Loan may include consolidation of existing debt on the Project Property so long as it does not improve the Third Party Lender's lien position on the existing debt, unless the debt is a previous Third Party Loan.

15. Businesses owned by ESOPs

    a. CDCs may make loans to an eligible business owned or controlled by an ESOP or equivalent trust.

    b. The ESOP must be in compliance with IRS, Treasury, and Department of Labor requirements. Prior to first disbursement, the CDC must obtain documentation that the ESOP or equivalent trust meets the requirements of all applicable IRS, Treasury, and Department of Labor regulations.

    c. The IRS prohibits ESOPs from guaranteeing a loan; therefore, SBA does not require the ESOP to guarantee the loan. All owners of the Applicant who hold an ownership interest in the small business outside the ESOP are subject to SBA's guaranty requirements.

    d. The application cannot be structured as an EPC/OC.

16. Ineligible Costs

    13 CFR § 120.884

Any costs not directly attributable to or necessary for the Project may not be paid with proceeds of the 504 loan.

17. Ineligible 504 Projects

    13 CFR § 120.881

    a. Relocation out of a Community – A Project cannot be approved under the 504 Loan Program if the Project involves the relocation of a business out of a community and will either have a net reduction of one-third of its jobs or cause a substantial increase in unemployment in any area of the country. An exception may be allowed if the CDC can justify the relocation as outlined in 13 CFR §§ 120.881(a)(1) and 120.881(a)(2); and

    b. Projects in foreign countries.

## D. 504 LOAN AND DEBENTURE TERMS AND CONDITIONS

The terms of the Third Party Loan are defined in 13 CFR § 120.921. Also see Paragraph B, Third Party Lender Participation of this Chapter.

1. Debenture Limits (Minimum and Maximum)

   13 CFR §§ 120.930 and 120.931

   Net Debenture Proceeds is defined in 13 CFR § 120.802 as the portion of Debenture proceeds that finance eligible Project costs (excluding administrative costs). The Gross Debenture is the Net Debenture Proceeds plus the eligible administrative costs. The Gross Debenture is subject to the following dollar limits and conditions:

   a. The minimum dollar amount for a debenture is $25,000. 13 CFR § 120.930(b)

   b. For all 504 Projects, the gross debenture is limited to an outstanding maximum balance of $5,000,000 in the aggregate for each small business concern, including its affiliates, except for Eligible Energy Public Policy Projects and Projects for Small Manufacturers in c. and d. below. SBA considers an EPC and an OC to be "one business" for this purpose. To calculate this limit, include only all SBA 504 loans, committed or outstanding, that the Applicant and its affiliates have received.

   c. Eligible Energy Public Policy Projects

      $5,500,000 maximum for each eligible project. However, the total outstanding Gross Debentures issued for a small business concern, including affiliates for Eligible Energy Public Policy Projects do not reduce the $5,000,000 limit for each small business concern for other 504 Projects. Eligible Energy Public Policy Projects include:

      i. Paragraph A.2.a.i of this Chapter: Projects for the reduction of existing energy consumption by at least 10%, and

ii. Paragraph A.2.a.ii of this Chapter: Renewable energy sources that generate more than 15% of energy used at Project Facility.

d. Projects for Small Manufacturers

$5,500,000 maximum for each eligible project, defined as a business with its primary NAICS Code in Sectors 31, 32, and 33, and all of its production facilities are located in the United States.

2. Loan Maturities

13 CFR § 120.933

a. Maturity of the 504 loan is 10, 20, or 25 years based upon the remaining useful life of the property being financed as follows:

i. A maximum of 25 years for real estate;

ii. A minimum of 10 years for machinery and equipment; and

b. When the Project includes both real estate and machinery and equipment, the maturity will be based on the asset category that constitutes the majority of loan proceeds.

c. A Third Party Loan must have a term of at least 7 years when the 504 loan is for a term of 10 years and 10 years when the 504 loan is for 20 or 25 years. (13 CFR § 120.921(a))

The amortization of the Third Party Loan shall not exceed that of the 504 loan.

3. Interest Rates

The interest rate for 10, 20, and 25 year 504 debentures is based on market conditions for long-term government debt at the time of sale. Most commonly, the 10-year Treasury Rate is used as a benchmark for the 20-year and 25-year debenture rates, and the 5-year Treasury Rate is used as a benchmark for the 10-year debenture rate. (13 CFR § 120.932)

(13 CFR § 120.921(b))

## E. CREDIT STANDARDS

The policies that make up SBA's credit standards begin with the requirements outlined in 13 CFR §§ 120.101 and 120.150. This section provides procedural guidance as to what the Lender should or must consider when analyzing any request for financial assistance that will be guaranteed by SBA.

Certified Development Companies (CDCs) must analyze each application in a commercially reasonable manner, consistent with prudent lending standards. The analysis must be acceptable to SLPC. On 504 loans, the cash flow of the Applicant is the primary source of repayment, not any expected recovery from the liquidation of collateral. Thus, if the CDC's financial analysis demonstrates that the Applicant lacks reasonable assurance of repayment in a timely manner

from the cash flow of the business, the loan request must be declined, regardless of the collateral available. The credit strengths and weaknesses of the proposed project must be identified and discussed by the CDC along with any mitigating factors.

1. CDC Credit Memorandum

   The CDC's credit memorandum must address the following:

   **a. Financial Reporting**

   i. The credit analysis must primarily focus on the highest level of financial statements available (Accountant Audited or Reviewed statements). Financial reporting is ordered by terms of thoroughness: (1) Audited Financial Statements, (2) Reviewed Financial Statements (Prepared to AICPA SSARS AR-C 90 standards), (3) CPA Compiled Financial Statements, and (4) Corporate Tax Returns.

   ii. In situations where a higher level financial statement is available, the credit memorandum must also include a review of the corporate tax return for eligibility.

   **b. TPL Underwriting**

   i. For any 504 project with total project costs of at least $5,000,000, the CDC must obtain and retain the Third Party Lender's underwriting analysis and include that analysis in the CDC credit memorandum when it is submitted to SPLC.

   ii. The CDC's credit memorandum must, at a minimum, summarize the TPL's assessment of repayment ability, collateral coverage, and material loan terms, and must identify any differences between the TPL's analysis and the CDC's conclusions.

   **c. Pro-Forma Balance Sheet Analysis**

   i. A pro-forma balance sheet is created from a current business balance sheet that has been adjusted for all changes in assets and liabilities as a result of the Project, including the Third Party Loan, 504 loan, other new debt, any required equity injection, the use of loan proceeds, and the costs of getting the loan(s) (such as fees and closing costs).

   ii. The pro-forma balance sheet analysis must include a complete debt schedule and discussion on the types and terms of the existing loans, debt, or credit facilities.

      a) This includes a review of the credit facilities that will be in place following the 504 transaction closing.

   iii. The CDC must identify and discuss issues resulting from any anomalies or variances on the balance sheet.

**d. Repayment Ability Analysis**

The analysis must address the following:

i. If the Applicant is meeting SBA Size Standards under the:

a) Alternative Size Standards – Include balance sheets, income statements, and Federal income tax returns for the previous 2 years, or the number of years the Applicant has generated revenue, whichever is less,

b) Industry Size Standard–- Include balance sheets, income statements, and Federal income tax returns for the previous 3 years, or the number of years the Applicant has generated revenue, whichever is less.

ii. For all 504 transactions, the repayment ability analysis must address debt service coverage. Debt Service Coverage (DSC) must be calculated on a historical basis using either the last fiscal year-end or an average of the last two fiscal year-end statements. The DSC ratio must be equal to or greater than 1.15:1.

a) The DSC ratio is defined as the operating cash flow (OCF) defined as earnings before interest, taxes, depreciation, and amortization (EBITDA) divided by the combined debt service post transaction. CDCs must assume interest-only payments on fully drawn lines of credit for this calculation.

i) Adjustments to cash flow:

The CDC must make prudent adjustments to the cash flow. When adjusting cash flow, the CDC must prepare a Global Cash Flow and include a justification for additions and subtractions to cash flow, such as the following:

(a) Rent payments;

(b) Unfunded capital expenditures;

(c) Non-recurring income;

(d) Distributions;

(e) Distributions for S-Corp taxes; and/or

(f) Ownership compensation.

iii. If the historical cash flow does not show sufficient debt service coverage after the effects of the SBA loan, the CDC must analyze projections in accordance with Subparagraph v., “Projection-based projects,” below.

iv. Balance sheet and income statement dated within 120 days prior to submission to SBA, including analysis of debt service coverage, aging of accounts receivable and accounts payable.

v. Projection-based projects:

If the historical cash flow does not show sufficient debt service coverage after the effects of the SBA loan, the CDC must analyze projections based on the following requirements:

a) For projection-based projects, the analysis must include a minimum of 2 years of projections.

b) The CDC must calculate the projected debt service coverage and provide the assumptions supporting the projected cash flow coverage.

c) The analysis must support and justify the reasonableness and attainability of the assumptions, including as applicable:

i) Justification for anticipated sales volume and/or revenue growth as a result of new product lines, sales channels, and new production facilities;

ii) Justification for any reduction in expenses; and

iii) Comparison to current industry trends.

d) If the projections show repayment in Year 2 but not in Year 1, sufficient liquidity must be shown to cover the shortfall in Year 1.

e) If applicable, the CDC must describe how the Applicant will make interest payments and pay for operations during construction.

**e. Borrower's Contribution**

i. The Borrower must contribute cash (or property acceptable to SBA obtained with the cash) or land (that is part of the Project Property) to the Project, or funds that were borrowed (subordinate to the Third Party loan and the 504 debenture, and, without SBA's written approval, may not be repaid at a faster rate than the 504 loan), in an amount equal to the following, excluding administrative costs:

a) All Borrowers must contribute at least 10%, which may be borrowed as long as it is subordinate to the Third Party Loan and the 504 debenture;

b) New businesses must contribute at least 15%. The Debenture will finance no more than 35% of the Project and at least 50% of the Project financing will be from banks or other financial institutions, state or local government, or foundations or other non-profit institutions.

c) Businesses with a Limited or Special Purpose Property:

i. Must contribute at least 15%, in which case the Debenture will finance no more than 35% of the Project and at least 50% of the Project financing will be from banks or other financial institutions, state or local government, or foundations or other non-profit institutions.

ii. Must contribute at least 20%, if the Project involves a new business 13 CFR § 120.910.

iii. If the Borrower contributes at least 20% under this Paragraph c), the Debenture will finance no more than 30% of the Project and at least 50% of the Project financing will be from banks or other financial institutions, state or local government, or foundations or other non-profit institutions.

iv. SBA allows Borrower's equity in equipment to be counted toward Borrower Contribution in 504 debt refinancing with and without expansion if the debt was originally used to acquire the specific equipment. The Borrower's equity in land and/or buildings and/or equipment previously acquired may be counted toward the Borrower's contribution if the land and/or buildings and/or equipment are part of the Project.

v. **CDCs must address whether the Project Property is Limited or Special Purpose in their credit memorandum and include an explanation of their conclusion**.

vi. Below is a list that contains examples of properties that SBA considers to be a Limited or Special Purpose Property. This list is not intended to be all-inclusive and SBA may determine that other properties meet the Limited or Special Purpose Property definition.

a) Amusement parks;

b) Bowling alleys;

c) Car wash businesses;

d) Cemeteries;

e) Cold storage facilities where more than 50% of total square footage is equipped for refrigeration;

f) Dormitories;

g) Farms, including livestock and dairy facilities;

h) Funeral homes with crematoriums;

i) Gas stations;

j) Golf courses;

k) Hospitals, surgery centers, urgent care centers, and other health or medical facilities;

l) Hotels, motels, and other lodging facilities;

m) Marinas;

n) Mines;

o) Nursing homes, including assisted living facilities;

p) Oil wells;

q) Quarries, including gravel pits;

r) Railroads;

s) Sanitary landfills;

t) Service centers (e.g., oil and lube, brake, or transmission centers) with pits and in-ground lifts;

u) Sports arenas;

v) Swimming pools;

w) Tennis clubs;

x) Theaters and auditoriums; and

y) Wineries.

d) If a Project will finance both a New Business and a Limited or Special Purpose Property, the Applicant must contribute at least 20% of the Project cost. The Debenture will finance no more than 30% of the Project and at least 50% of the Project financing will be from state or local government, banks or other financial institutions, foundations or other non-profit institutions.

ii. The additional Borrower's contribution will reduce the SBA's portion of the financing.

iii. The Borrower's equity in land and/or buildings previously acquired may be counted toward the Borrower's contribution if the land and/or buildings are part of the Project.

iv. If the Borrower's contribution is borrowed:

a) Any lien position on the Project Property must be subordinate to the 504 loan;

b) Only in situations where the borrowed contribution is collateralized by the Project Property, Borrower may not pay the loan for its contribution at a faster rate than the 504 loan (13 CFR § 120.912) unless it is approved in writing by the D/FA or designee; and

c) If the borrowed contribution is collateralized by assets other than the Project Property, the Borrower must demonstrate repayment of the loan for its contribution from the cash flow of the business or other sources.

**f. Additional Borrower's Contribution and/or Collateral**

The required Borrower's contribution, as set forth in Paragraph 1.c. immediately above, and collateral, as set forth in Paragraph 2.a. of this Chapter below, on SBA 504 loans are the minimums required by policy. However, in some cases it may be appropriate to consider additional Borrower contribution and/or collateral to mitigate the credit weaknesses of a proposed project. Examples of such credit weaknesses include:

i. Marginal historical or projected cash flow;

ii. Limited working capital;

iii. Recent significant increase in debt;

iv. Restricted or limited customer base;

v. Limited or no net worth.

This list is not intended to be all-inclusive and SBA may determine that other circumstances necessitate additional Borrower contribution and/or collateral.

**g. Global Cash Flow Analysis**

The following may be included in the global cash flow analysis. Note: Repayment ability is determined based on the operating company cash flow analysis.

i. Personal discretionary income analysis with outside income:

a) Any income not generated from the Applicant, such as spousal income, affiliate income, or interest income is considered outside income.

b) Outside income can be used to offset personal obligations and living expenses. However, outside income may not be added to the business cash flow because repayment ability analysis must be based on the cash flow of the business.

ii. Rental Income

Anticipated cash flow from rental income from the Project Property may be included in the global cash flow analysis. However, it must not be included in the repayment ability analysis.

**h. Independent Studies or Reports**

Reports prepared independently of the small business may be beneficial in mitigating any weaknesses identified in the credit analysis. Examples of these independent studies/reports may include:

i. Feasibility studies;

ii. Hospitality facility assessment reports;

iii. Energy audits; and

iv. Franchise (as defined by FTC) assessment reports.

**i. Feasibility Studies**

SBA has the regulatory authority to request a feasibility study when it is needed to further understand the small business type and market conditions at the project location. The SLPC Director will request a feasibility when appropriate. The following may cause SBA to request a feasibility study:

i. Market saturation by industry type and location;

ii. Unique market concept;

iii. Highly specialized Project property;

iv. Project size disproportionate to size of community it will serve; or

v. Significant rapid growth of the Applicant and/or affiliate group with a corresponding increase in undisbursed and/or unseasoned debt.

**j. Ratio Analysis**

A ratio analysis of the Federal tax returns and interim financial statements including comments on any trends and a comparison with industry averages. The analysis must include a review of calculations (based on the pro-forma Balance Sheet and historical and projected Income Statements) for the following financial ratio benchmarks:

i. Current Ratio;

ii. Debt/Tangible Net Worth;

iii. Debt Service Coverage;

**iv.** Any other ratios that are relevant for the business/industry (e.g., inventory turnover, receivables turnover, and payables turnover, etc.) including discussion of the CDC's comparison to industry trends.

**k. Owners or Manager's Experience**

A discussion of the owners' and managers' relevant experience in the type of business, as well as their personal credit histories. A description and history of the business including:

i. Nature of the business;

ii. Length of time in business under current management;

iii. Depth of management experience in the industry or a related industry;

iv. Brief description of the business's management team including principal's involvement in the daily onsite management of the business or how the daily operations will be managed if the principals are not there on a daily basis.

**l. Collateral Analysis**

The CDC must discuss the collateral and lien position. CDC must disclose any deed restrictions on the project property.

**m. Life Insurance Analysis**

The CDC must include a discussion of its analysis whether life insurance is required in accordance with Section A, Ch. 5 Para. C.5, Life Insurance. If life insurance is required, include the calculation of the amount required. If the CDC determines the viability of the business is not tied to an individual, include an explanation of this determination.

**n. Credit Reports**

CDCs are required to obtain and review credit reports for the small business concern applying for the loan, all owners who are guarantors and affiliates who are guarantors. The analysis must include a discussion of the Applicant's credit history, including a review of business credit reports and any experience the CDC may have with the Applicant. Credit reports are not required on non-guarantor affiliates. Credit reports must be current within 90 days of loan approval.

**o. Current on Taxes**

The CDC must verify the Applicant is current on all Federal, State, and local taxes, including but not limited to income taxes, payroll taxes, real estate taxes and sales taxes. For more information, see Section A, Ch. 1, Para. E, Types of Ineligible Businesses.

**p. No Prior Loss to the Government or Delinquent Federal Debt**

SBA may not approve a 504 loan to an Applicant who has a Prior Loss to the government or Delinquent Federal Debt. For more information, see Section A, Ch. 1, Para. E, Types of Ineligible Businesses.

**q. Payment Delinquencies, Liens and Bankruptcies**

The CDC's credit memorandum must include a discussion on payment delinquencies, judgments, liens, bankruptcy filings, pending litigation, Federal or state tax filings, or other relevant information from the credit reports.

**r. Affiliate Financial Statements**

The last 2 fiscal year-end financial statements and/or Federal income tax returns of affiliates (or 3 years, if the Industry Size Standard is used to qualify for SBA Size Standard) should be included in the CDC's submission to SLPC. The CDC must also provide an analysis of these returns and statements including a complete debt schedule and discussion on the types and terms of the existing loans, debt, or credit facilities.

**s. Miscellaneous Matters that the CDC Must Address in the Credit Memorandum**

i. Applicant meets requirements for SBA financial assistance under SBA Loan Program Requirements.

ii. The Interim Loan (if any):

a) Does not cover the Applicant's contribution;

b) Source has the experience and qualifications to monitor properly all Project construction and program payments

c) Source is not:

i) From any SBA Program, directly or indirectly; or

ii) The Applicant or an Associate of the Applicant; and

d) Terms and conditions of the financing are acceptable.

iii. The Third Party Loan:

a) Is at least as much as the 504 Loan (net debenture proceeds);

b) Has a term of at least 7 years for a 10year debenture and at least 10 years for a 20-year or 25-year debenture;

c) Interest rate is reasonable.

iv. Any financing provided by the seller of the Project Property is subordinate to the 504 loan and may not be prepaid without SBA consent.

v. None of the 504 loan proceeds are being used to provide or refinance funds used for payments, distributions, or loans to Associates of the Applicant.

vi. The Debenture Pricing.

vii. If Applicant is an Eligible Passive Company:

a) The EPC and OC both meet requirements for SBA financial assistance under SBA Loan Program Requirements;

b) The EPC will use the 504 loan proceeds to acquire or lease, and/or improve or renovate real or personal property (including eligible refinancing) that it leases 100% to the OC;

c) The lease between the EPC and the OC will:

i) Be in writing;

ii) Have a remaining term at least equal to the term of the loan (including options to renew exercisable solely by the OC);

iii) Be subordinated to SBA's lien on the property; and

iv) Have rents that will be assigned as collateral for the loan.

viii. The Gross Debenture amount does not exceed the amounts established by SBA Loan Program Requirements.

ix. The Applicant's use of proceeds complies with SBA Loan Program Requirements.

x. Whether the loan is for the following special purpose or the Applicant is or does one of the following: Disabled Assistance Loan Program (DAL), Energy Conservation, Qualified Employee Trusts (ESOP), or Pollution Control Program. If so, PCLP CDCs may not approve the loan under their delegated PCLP authority.

2. Collateral and Appraisals

Note: Environmental Policies and Procedures are located in Section A, Ch. 5, Para. E.

**a. Collateral**

i. SBA's 504 Collateral Policy 13 CFR §120.934

When assessing the adequacy of collateral, the CDC must consider the impact that covenants and other restrictions recorded against the collateral may have on its value and marketability. The CDC must document this analysis in the file. Examples of items to review include:

a) Deed restrictions, covenants, easement provisions, reversionary interests, subordinations, leases and options and other provisions that restrict the use of the property for the benefit of a third party (note: certain deed restrictions pertaining to the use of the property, which are intended to protect the health and safety of occupants, may be acceptable, e.g., deed restrictions based upon environmental concerns including restrictions on residential use, use as a day care center for children or seniors, use as a school, or use as a hospital); and

b) Engineering Controls that require the small business concern or subsequent owners to install costly devices or structures such as extraction wells or subsurface barrier walls prior to constructing a building, remodeling, or otherwise improving the property.

c) Environmental Indemnification provisions that run with the land are not eligible and must be removed or waived as to the Federal Government. CDC should review all other Non Environmental indemnification provisions as to their impact as to the value of the collateral and send the write up and a copy of the indemnification to EnvironmentalReviews@sba.gov for clearance.

d) CDC must review all real estate title documents (i.e., deeds or other recorded documents) that run with the land to determine if the real property collateral is subject to any non-environmental open-ended (indefinite) indemnification provisions (other than Environmental Indemnification provisions covered in (c) above). Open-ended indemnification provisions are those where someone has a right to indemnification from subsequent owners of the Property (e.g., SBA/ SBA Lender after acquiring Property through foreclosure or other means). If the property is subject to a "non-environmental open-ended indemnification provision" then:

i) CDC must attempt to obtain (from benefiting party) a written waiver and release of right to indemnification that the provision is not enforceable as to the Federal Government or as to the U.S. Small Business Administration, and record such waiver and release in the land title records, prior to loan closing.

ii) If CDC cannot obtain such waiver, CDC must submit a 327 action: (a) identifying the title provision, and (b) documenting its attempts at obtaining a recorded waiver, to the SLPC for resolution.

SBA usually takes a second lien position on Project Property but may have a shared lien (pari passu) with the Third Party Lender.

ii. Adequacy of Collateral:

a) SBA's second lien position will generally be considered adequate. SBA may consider other factors in determining the adequacy of SBA's collateral including but not limited to the following:

i) Strong, consistent cash flow that is sufficient to cover the debt;

ii) Demonstrated, proven management;

iii) The Applicant has been in operation for more than 2 years; and

iv) The proposed Project is a logical extension of the applicant's current operations.

b) Because leasehold improvements provide minimal collateral value, the CDC must consider requiring additional collateral.

c) Do not encumber assets or require additional contributions that the Borrower needs to sustain ongoing operations. Taking additional collateral with minimal liquidation value only serves to limit the Borrower's ability to obtain additional short-term financing while offering little or no additional protection to SBA.

d) If the loan is not fully collateralized by business assets, available personal assets must be pledged to secure the guaranty. See Section A, Ch. 5, Para. A, Guaranties, for more information.

e) Lien position on real estate is generally evidenced by a title insurance policy. If the title insurance policy contains a clause requiring arbitration or a clause allowing either party to demand arbitration in the case of a dispute, an endorsement to the policy must be obtained deleting that condition. If the policy requires that both parties agree to arbitration, no endorsement is necessary.

iii. Third Party Loan:

a) The Third Party Lender usually has a 1st lien on the Project Property, and SBA cannot guarantee these loans. (13 CFR § 120.920)

b) When the Third Party Lender is the property seller, the Third Party Loan must be subordinate to the 504 loan except under the following circumstances (13 CFR § 120.923):

i) The Borrower assumes an existing note as part of the total financing;

ii) The FDIC has carry-back financing; or

iii) The property is classified as "Other Real Estate Owned" (OREO), by a national bank, a State-chartered, or other federally-regulated lender and the property is of sufficient value to support the 504 loan. For more information on eligibility of OREO property, see Section A, Ch. 3, Para. A.1.g.

c) SBA's lien position must not be subordinate to loans made from the proceeds of a tax-exempt obligation.

iv. Mixed Use Collateral:

When one 504 debenture finances both real estate and significant shorter term assets, such as machinery and equipment and furniture and fixtures, the CDC should consider the following:

a) Taking, along with the Third Party Lender, lien positions based upon proportional shares in the financing of the Project;

b) Taking a 1st lien position on the shorter term assets. SBA requires at least a 2nd lien position unless there is a lien from an existing 504 loan on the assets;

c) Requiring additional equity or collateral; or

d) Removing the shorter term assets from the Project and have them financed by another source.

**b. Appraisals**

13 CFR § 120.160(b)

i. Commercial Real Estate:

a) Appraisals and Evaluations:

i) SBA requires a real estate appraisal if the estimated value of the Project Property is greater than $500,000.

ii) If the estimated value of the Project Property is $500,000 or less:

(a) The CDC must obtain an appraisal under the following circumstances:

(i) Equity in land owned for 2 years or more is being contributed as part of Borrower's contribution;

(ii) The real estate is Third Party Lender's OREO property (see Section A, Ch. 3, Para. A.1.g., for more information);

(iii) If the loan finances a transaction involving parties with a close relationship (for example, transactions between existing owners or family members);

(iv) The seller of the property is carrying back a loan that is part of the Borrower's contribution;

(v) When the project includes a change of ownership; or

(vi) If SBA or the CDC otherwise concludes that an appraisal is necessary to appropriately evaluate creditworthiness.

(b) If an appraisal is not required under the preceding paragraphs, the CDC must obtain an appropriate evaluation of the Project Property being acquired with the loan proceeds that is consistent with safe and sound banking practices. Evaluations are not required to be performed in accordance with USPAP or by a State licensed or certified appraiser but should be consistent with the Interagency

Guidance Appraisal and Evaluation Guidelines and the Interagency Advisory on the Use of Evaluations in Real Estate-Related Financial Transactions, issued by the Federal Banking Regulators.

b) The appraiser must be:

i) Independent and have no appearance of a conflict of interest (such as a direct or indirect financial or other interest in the property or transaction, independent of the loan production function, and not involved in the approval of the transaction); and

ii) Either State-licensed or State-certified with the following exception: when the Project Property's estimated value is over $1,000,000, the appraiser must be State-certified.

c) The "Appraisal Report" must be prepared in compliance with the Uniform Standards of Professional Appraisal Practice (USPAP) and dated no more than twelve months prior to the date of application.

d) In order for the appraiser to identify the scope of work appropriately, the appraisal must identify SBA as the client or an intended user of the appraisal, as those terms are defined in the Uniform Standards of Professional Appraisal Practice (USPAP). The CDC may also be identified as the client or an intended user. It is acceptable to SBA if the appraisal identifies the Third Party Lender as the client and SBA as intended user. The CDC may not use an appraisal prepared for the applicant. The cost may be passed on to the Borrower.

e) If the loan will be used to finance new construction or the substantial renovation of an existing building, the appraisal must estimate what the market value will be at completion of construction. ("Substantial" means rehabilitation expenses of more than one-third of the purchase price or fair market value at the time of the application.) After construction is completed, CDC must obtain a statement from the appraiser, general contractor, project architect, or construction management firm that the building was built with only minor deviations (if any) from the plans and specifications upon which the original estimate of value was based. If the CDC cannot obtain such a statement, then the CDC cannot close the loan without the Sacramento Loan Processing Center's (SLPC) prior written permission.

f) If the loan will be used to acquire an existing building that does not require construction, the appraiser should estimate market value on an as-is basis. If the appraiser estimates the value other than on an as-is basis, the narrative must include an explanation of why the as-is basis was not used.

g) If the appraisal engagement letter asks the appraiser for a business enterprise or going concern value, the appraiser must allocate separate values to the individual components of the transaction including land, building, equipment, and business (including intangible assets).

h) When the collateral is a Special Purpose Property, the appraiser must be experienced in the particular industry.

i) An appraisal must be submitted and approved by the SLPC (except on Delegated loans) prior to closing. If the appraisal comes in at less than 90% of the estimated value, the debenture must be reduced or, if available, the CDC must secure additional collateral or additional investment from the Borrower and/or guarantors that will be added to the required Borrower's Contribution and will be sufficient to address the gap in value. If additional collateral or additional investment is not available, but the applicant demonstrates strong, consistent cash flow sufficient to support the debt, then the SLPC can approve the appraisal and the CDC may close the loan.

j) An appraisal must be submitted to the SLPC with the application under the following circumstances:

i) Equity in land owned for 2 years or more is being contributed as part of Borrower's contribution;

ii) The real estate is Third Party Lender's OREO; or

iii) The Project will finance a transaction involving parties with a close relationship (for example, transactions between existing owners or family members).

iv) The seller of the property is carrying back a loan that is part of the Borrower's contribution.

v) For both non-arm's length transactions and change of ownership projects, the property must appraise for 100% of the estimated value. The purchase price is limited to the lesser of the As-Is appraised value or the purchase price of 504 eligible fixed assets.

ii. Equipment Appraisal:

SBA requires that an equipment appraisal be obtained when used equipment is part of the Project and is either being purchased from someone other than an equipment dealer or being refinanced. The equipment appraisal needs to be a written document from a person that is qualified to provide a valuation, is independent of the transaction, and has performed an on-site inspection of the equipment. The appraisal must be dated no more than twelve months prior to the date of the application.

iii. Non-commercial real estate or real estate securing a personal guaranty:

SBA has no specific appraisal requirements for non-commercial real estate (such as a residence) or real estate (commercial or non-commercial) taken as collateral to secure a personal guaranty.

## F. SUBMISSION OF LOAN APPLICATION

1. Processing Methods

All 504 loans are processed in the SLPC.

a.

b. Non-delegated (without the use of the Abridged Submission Method): When a CDC submits an SBA 504 application under the non-delegated processing method, the CDC submits the application and supporting documents to SBA through the SBA Loan System. SBA will make the final determination as to the eligibility of the Applicant, use of proceeds, the credit decision, including adequacy of collateral pledged, structure of the loan, and the Borrower's contribution of the Applicant.

c. Abridged Submission Method (ASM): ASM is a streamlined loan application processing procedure, which does not involve the exercise of any delegated authority.

d. Accredited Lenders Program (ALP): SBA delegates to ALP CDCs increased authority to process, close and service 504 loans. (13 CFR § 120.840) CDCs processing loans under their ALP authority will use one of the processing methods as described in this Paragraph 1.a. or b., or their ALP Express authority for qualifying loans as described in 1.d.

e. ALP Express: ALP CDCs in good standing may underwrite, approve, close, and service ALP Express Loans. An ALP Express Loan is a 504 loan in an amount that is not more than $500,000 which has been made by an ALP CDC and designated by the ALP CDC as an ALP Express Loan during submission. SBA will not review the credit decision made by the ALP CDC for an ALP Express Loan. However, the ALP Express Loan is subject to final approval by the Sacramento Loan Processing Center (SLPC) as to eligibility, as described in this paragraph 3.e. There is no loan loss reserve requirement for loans made under ALP Express delegated authority.

f. PCLP CDC: Under the Premier Certified Lenders Program (PCLP), SBA delegates to PCLP CDCs increased authority to process, close, service and liquidate 504 loans, and may also give PCLP CDCs increased authority to litigate 504 loans (13 CFR § 120.845). Loans processed under PCLP CDC authority are subject to the same loan terms and conditions as other 504 loans, but SBA

delegates to the PCLP CDC all loan approval decisions except certain eligibility issues. The SOP indicates where PCLP CDCs are required to process 504 loans using non-delegated processing. PCLP CDCs may decide to process an ALP Express Loan under their status as an ALP CDC instead of as a PCLP CDC, thereby not requiring the CDC to comply with Loan Loss Reserve Fund requirements for that loan. A PCLP CDC that decides to process a loan as an ALP Express Loan may only use ALP Express authorities, not PCLP authority, for that loan.

2. Contents of a 504 Loan Application

The CDC must maintain the following documents and any that support the CDC's credit decision in the CDC's loan files. CDC files must be available for review by SBA at any time.

a. The CDC completes or obtains the following:

iv. SBA Form 1244, "Application for Section 504 Loan." CDC must list in the SBA Loan System 100% of the total direct and indirect ownership of the Applicant. The ownership percentage of married spouses and minor children must be combined. Additional sheets may be attached to the Form 1244 if necessary. The Applicant is not eligible for a 504 loan if any Associate (as defined in 13 CFR § 120.10) responds "Yes" to the question regarding criminal history on SBA Form 1244.

v. CDC credit memorandum, in accordance with Paragraph E.1, CDC Credit Memorandum, of this Chapter.

vi. For any 504 project with total project costs of at least $5,000,000, the CDC must obtain and retain the Third Party Lender's underwriting analysis and incorporate it into the CDC credit memorandum in accordance with Paragraph C.1.b. of this Chapter

vii. Copies of key cost documents such as contractor costs, estimates, vendor quotes for machinery and equipment, etc., as well as an itemized listing of estimated professional fees (e.g., appraiser, architect, legal, etc.). Full or partially executed purchase/sale agreements must be included.

viii. Independent appraisal for project real estate as required by Paragraph 2.b. of this Chapter.

ix. Environmental analysis in accordance with Section A, Ch. 5, Para. E, Environmental Policies and Procedures, if applicable.

x. SBA Form 2481, "Historic Property Borrower Certification," if applicable, in accordance with Section A, Ch. 5, Para. D., Historic Properties.

xi. Letter of intent/term sheet from the Third Party Lender stating the terms and conditions and the reason why it will not finance the entire project.

xii. Completed SBA Form(s) 159, "Fee Disclosure Form and Compensation Agreement," if applicable, in accordance with Section A, Ch. 4, Para. E.7, Disclosure of Fees – SBA Form 159.

xiii. For "Debt Refinance With Expansion" projects:

a) Copies of the most current debt and lien instruments;

b) Transcript of account or equivalent for any debts being refinanced; and

c) Certifications required for refinancing.

xiv. For "Debt Refinance Without Expansion" projects:

a) Copies of the transcript(s) of account or equivalent for any debts being refinanced; and

b) Certifications required for refinancing.

xv. SBA Form 413, Personal Financial Statement (or CDC's equivalent form), signed and dated within 90 days, as well as copies of Federal income tax returns for the last 1 year, for each:

a) Proprietor, partner, or stockholder with 20% or more ownership of the Applicant or the OC, if the Applicant is an EPC; and

b) If different than a) immediately above, each owner with 20% or more ownership of the EPC; and

c) Any proposed guarantors, except Supplemental Guarantors.

xvi. Credit reports , dated within 90 days, for:

a) Applicant;

b) Proprietor, partner, or stockholder with 20% or more ownership of the Applicant, and, if requested by SLPC, Key Employee;

c) Affiliates; and

d) Guarantors.

xvii. If the Applicant is meeting SBA Size Standards under the:

a) Alternative Size Standard – Include balance sheets, income statements, and tax returns for the previous 2 years or the number of years the Applicant has generated revenue, whichever is less;

b) Industry Size Standard–- Include balance sheets, income statements, and tax returns for the previous 3 years, or the number of years the Applicant has generated revenue, whichever is less.

xviii. A balance sheet and income statement dated within 120 days prior to submission to SBA and an aging of the accounts receivable and accounts payable. If the Applicant is a new business, provide a proforma balance sheet with a description of assumptions attached.

xix. Where appropriate, projected annualized income statements for the first 2 years after loan closing including a description of assumptions.

xx. For a new business, a monthly cashflow analysis for the first 12 months of operations or for 3 months beyond the breakeven point (whichever is longer) together with a description of assumptions.

xxi. Schedule of debts including the original date and amount, monthly payment, status of the loan (current, delinquent, paid in full, or charged off), interest rate, present balance owed, maturity, to whom payable, and collateral securing the loan for each short-term and long-term loan that the business currently has outstanding or has planned for the next 12 months (other than the 504 loan).

xxii. Schedule of any previous government financing received by the Applicant or any affiliated company of the Applicant as well as any Associate (as defined by 13 CFR § 120.10) or principal of the Applicant. Include the name of the Agency, the original date and amount, the outstanding balance, status of the loan (current, delinquent, paid in full, or charged off), and collateral securing the loan.

xxiii. Names of affiliated or subsidiary businesses as well as the last 2 fiscal year-end financial statements and/or Federal income tax returns for the last 2 years (or 3 years, if the Industry Size Standard is used to qualify for SBA Size Standard).

xxiv. IRS Form 4506-C, IVES Request for Transcript of Tax Return or IRS Form 8821, Tax Information Authorization. CDCs must select the same type of form the CDC used when verifying borrower financial information.

xxv. Documentation of U.S. National in accordance with Section A, Ch. 1, Para. F., “Citizenship and Residency Requirements”. CDCs must receive verification of the status of each U.S. National. CDC must document their findings of the review proving a U.S. National’s status (birth certificate and/or passport) in the loan file, and enter the U.S. National’s Social Security Number on the Application in the SBA Loan System.

xxvi. Not required until loan closing: IRS Transcripts and complete verification of borrower financial information.

b. Due to the certification on SBA Form 1244, original signatures from the Applicant are not required on the following:

i. Balance sheet, income statement, and Federal income tax returns (business or personal);

ii. Aging of the accounts receivable and accounts payable listed;

iii. Financial statements and/or Federal income tax returns for affiliated entities and subsidiary businesses; and

iv. SBA Form 413, Personal Financial Statement or CDC's equivalent, dated within 90 days of loan approval.

3. Submission of Application

a. Detailed guidance on the SBA Loan System submission process can be found in the 504 User Guide for submitting loan applications, posted on SBA's website. CDCs may choose to either use a vendor solution that integrates with the Capital Access Financial System (CAFS) loan platform or manually use the SBA Loan System web screens. Documents greater than 250MB must be separated into multiple documents. The system does not support uploads greater than 250MB.

b. Regardless of the processing method used:

i. CDCs must retain the full application in its file.

ii. One hundred percent of the Applicant's ownership and percentage of ownership must be disclosed in the SBA Loan System.

c. Non-delegated and not using ASM

CDCs processing a loan under non-delegated authority and not using ASM must submit all items in Paragraph 2.a. above into the SBA Loan System for loan approval by SLPC.

d. ASM

i. Submit items in 2.a.i. through 2.a.xiv above into the SBA Loan System for loan approval by SLPC.

ii. Applications for projects that result in change of ownership or transactions between close family members cannot be processed under ASM.

e. ALP Express Loans

i. The ALP CDC must upload into the SBA Loan System the ALP Express Loan application, including the exhibits identified in the SBA Form 1244 required for ALP Express Loans. ALP CDC must retain all other exhibits in the loan file.

ii. The ALP CDC must indicate on SBA Form 1244 (page 10) that it is submitting the loan as an ALP Express Loan. If the ALP CDC does not designate on SBA Form 1244 that the ALP CDC is using the ALP Express

submission method, SBA will process the loan as a standard 504 loan.

iii. SLPC will review each complete ALP Express Loan application for eligibility and communicate any eligibility issues to the CDC for resolution. ALP CDCs must continue to obtain SBA's approval involving certain program eligibility requirements, including but not limited to those requirements involving historic properties, all environmental documents, and businesses involving activities of a prurient sexual nature.

iv. SLPC will not review the ALP CDC's credit decisions for any application submitted using the ALP Express delegated authority. SLPC will review the appraisal, as needed, to determine eligibility. SLPC will not review the life insurance requirements, which is a credit and collateral responsibility of the ALP CDC.

v. ALP CDCs must submit to the SLPC for review and approval any servicing action that the ALP CDC proposes prior to closing that may affect the eligibility of the borrower or the ALP Express Loan.

vi. Once SLPC determines the applicant and the loan are eligible and that SBA funds are available for the loan, the SLPC will issue an SBA Loan Number and will update the SBA Loan System with the Terms and Conditions of the 504 Loan.

vii. ALP Express Authority may not be used in the following circumstances:

a) Previously Declined/Withdrawn Loans: ALP Express authority may not be used to process 504 loans previously submitted to SBA and withdrawn by the CDC or declined or otherwise not approved by SBA. An ALP CDC must review the borrower certification on SBA Form 1244 to ascertain whether the 504 loan was previously submitted to SBA and confirm with SLPC whether the loan was previously withdrawn by the CDC or was declined or otherwise not approved by SBA.

b) Exceptions to Policy: Any 504 loan that will need an exception to policy may not be processed as an ALP Express Loan, and must be submitted to SBA through SLPC in accordance with this SOP.

c) Increase over $500,000: An ALP Express Loan may not be increased over $500,000. Any increase above $500,000 would require the ALP Express Loan to be cancelled and resubmitted as a non-delegated loan through SLPC.

f. Premier Certified Lenders Program (PCLP) Loans

The PCLP CDC must complete and upload the following documents into the SBA Loan System within 15 business days after debenture funding:

i. The final executed SBA Terms and Conditions (updated to reflect the final terms of the loan);

ii. SBA Form 1244, "Application for Section 504 Loan." One hundred percent of the Applicant's ownership and each owner's percentage of ownership must be disclosed on SBA Form 1244 (additional sheets may be attached to the Form 1244 if necessary).

4. Reconsideration of declined non-delegated 504 Loans (13 CFR § 120.193):

a. If the CDC believes the reason(s) for decline have been overcome, a request for reconsideration may be submitted along with a detailed written explanation of how the Applicant has overcome the reason(s) for decline. Lender must submit a request for reconsideration to the SLPC within 6 months of the date of decline. Any request submitted more than 120 days after the date of decline must include current financial statements.

b. If a request for reconsideration is declined twice by the SLPC, a third reconsideration may be requested from the D/FA or designee, whose decision is final. The request to the D/FA or designee must be submitted to the SLPC and must include a copy of the Center's decline letter and include additional information that specifically addresses the reason(s) identified for decline and how the Applicant has overcome those reason(s). The SLPC will forward the request to the D/FA or designee for a final decision.

# CHAPTER 2: SBA TERMS AND CONDITIONS THROUGH DISBURSEMENT

## A. SBA TERMS AND CONDITIONS

The SBA Terms and Conditions is SBA's agreement between the SBA and the CDC providing the terms and conditions under which SBA will issue a debenture.

1. Loan Conditions (13 CFR § 120.160):
    a. SBA establishes the wording for the standard 504 SBA Terms and Conditions.
    b. The SBA-authorized SBA Terms and Conditions for 504 loans must use the pre-approved conditions that are found in the Boilerplate.
    c. The party responsible for drafting the SBA Terms and Conditions is determined by the program the loan is processed under:
        i. Regular and ALP: The CDC drafts the SBA Terms and Conditions and the SBA finalizes and executes and sends to the CDC for execution
        ii. PCLP: CDC drafts and executes on SBA's behalf
    d. SBA counsel must review and approve any SBA Terms and Conditions with the following exception. When processing a loan under PCLP lending authority, PCLP CDCs may develop the SBA Terms and Conditions and use them without prior SBA approval, provided they are only used one time. Whenever a PCLP CDC develops and uses a non-standard condition, an explanation for its development must be in the loan file.
2. Disbursement Period, Interest Rates and Loan Maturity:
    a. Disbursement Period: The loan must be disbursed within 48 months from the date of approval, unless an exception to policy is approved and an extension is granted by SBA through the OFPO/SLPC, with concurrency by SBA CFO to confirm funding authority. For Debt Refinance without Expansion, the loan must be disbursed within 9 months from the date of approval. For Debt Refinance without Expansion, SBA may grant an extension not to exceed 15 months. When appropriate, SLPC will also refer extension requests to OFA for concurrency with OGC and the CFO.

        **SBA will track the approved time frame for loans and automatically cancel undisbursed dollars**. The Denver Finance Center (DFC) will make a reasonable effort to mail an initial message to the CDC approximately 3 months prior to taking action on undisbursed funds. The message will inform the CDC of the undisbursed dollar amount and will provide a date on which the dollars will be automatically cancelled. After the 3-month message has expired, DFC will make a

reasonable effort to mail a second message on the day the automatic cancellation is processed.

To request an extension of the disbursement period, a CDC must submit the request through the SLPC as a 327 action and must include the following:

i. The reason for the extension, with a detailed timeline for project completion and funding.

ii. A determination of no adverse change.

iii. Updated financial statements dated within 120 days (or 90 days for personal financial statements) of the request and analysis thereof.

iv. Documentation to demonstrate how the project sources and uses have been adjusted for any increases in project costs.

For loans processed under a CDC's PCLP authority, items listed under Section C, Ch. 1, Para. F.2.a.i.-iv. must be submitted directly through the SBA Loan System with notification to the SLPC for review and consideration.

b. Interest Rate: The interest rate for 10, 20, and 25 year 504 debentures is based on market conditions for long-term government debt at the time of sale. 13 CFR § 120.932

c. Maturity is 10, 20, or 25 years based upon the remaining useful life of the property being financed, in accordance with Ch. 1, Para. D.2, Loan Maturities.

3. Interim and Third Party Lender Requirements:

CDC must insert the names of the Interim and Third Party Lenders and the amounts of the loans into the SBA Terms and Conditions.

4. Insurance Requirements: Lender must ensure all appropriate insurance requirements are included in the SBA Terms and Conditions.

5. IRS Tax Transcript/Verification of Financial Information:

The IRS Tax Transcript/Verification of Financial Information process must be completed in accordance with Section A, Ch. 5, Para. B, IRS Tax Transcript/Verification of Financial Information.

6. Standby Agreements:

d. SBA Form 155,"Standby Agreement." CDC may use SBA Form 155 or its own equivalent standby agreement form. A copy of the note must be attached to the standby agreement.

e. Standby Creditor must subordinate any lien rights in collateral securing the Loan to CDC's rights in the collateral and take no action against Applicant or any collateral securing the Standby Debt without CDC's consent.

7. Assignment of Lease and Landlord's Waiver:

   If applicable, the SBA Terms and Conditions must include conditions for assignment of lease and landlord's waiver.

8. Construction Loan Provisions:

   a. In the construction of a new building or an addition to an existing building, the CDC must obtain:

      i. Evidence of compliance with the ""National Earthquake Hazards Reduction Program Recommended Provisions for the Development of Seismic Regulations for New Building"" (NEHRP), or a building code that has substantially equivalent provisions. (13 CFR § 120.174)

         a) The NEHRP provisions may be found in the American Society of Civil Engineers (ASCE) Standard 7 and the International Building Code.

         b) Examples of evidence include a certificate issued by a licensed building architect, construction engineer or similar professional, or a letter from a state or local government agency stating that an occupancy permit is required and that the local building codes upon which the permit is based include the Seismic standards.

      ii. The SBA Terms and Conditions must address the NEHRP provision when any of the use of proceeds options selected includes construction financing, including leasehold improvements. If the leasehold improvements made with loan proceeds will become permanently affixed to any structure on the leased premises, then they must comply with the NEHRP. If the leasehold improvements are only temporary, they do not need to comply with the NEHRP. Accordingly, if the Applicant can demonstrate that the leasehold improvements will be temporary, CDC may request modification of the SBA Terms and Conditions to remove the NEHRP provision in accordance with Paragraph B., Modifying the SBA Terms and Conditions, of this Chapter. The CDC must certify that the Project was completed in accordance with the final plans and specifications unless a minor portion of the project has been escrowed for a valid reason. (13 CFR § 120.891)

   b. If the interim financing comes from a CDC, the following additional conditions must be required in the SBA Terms and Conditions:

      i. Mortgages must be recorded prior to beginning construction.

      ii. Inspections must be made by a qualified engineer, appraiser, or other party satisfactory to SBA prior to all progress disbursements.

      iii. The Applicant must furnish a firm construction contract to the CDC from an acceptable contractor at a specified price, including a provision that no

material changes are to be made without the prior written consent of the CDC;

iv. The contractor must furnish builder's risk and workers' compensation insurance;

v. One complete set of plans and specifications of the proposed construction must be submitted to the CDC;

vi. Where the CDC or the Applicant is to inject funds into the construction project, these funds must be used prior to the disbursement of the interim financing;

vii. The CDC must make and document periodic inspections of construction; and

viii. When loan funds will be used to improve buildings on leased land, assignment of the lease must be obtained.

9. Special Provisions for Personal Property, Equipment and Fixtures as Collateral. If the collateral for the loan includes equipment and/or fixtures:

   a. The CDC must obtain a list of all equipment and fixtures that are collateral for the loan.

   b. For items with a unit value of $5,000 or more, the list must include a description of the equipment/fixture and serial number, if applicable.

   c. The list should be included in the collateral description (Item 4. COLLATERAL) on the UCC-1 Financing Statement.

10. Certifications of the CDC:

    The certifications required of the CDC are listed on SBA Form 2101, "CDC Certification."

11. Certifications of the Borrower:

    The certifications required of the Borrower are listed on SBA Form 2289, "Borrower and Operating Company Certification."

12. Certifications of the Interim Lender:

    The certifications required of the Interim Lender are listed on SBA Form 2288, "Interim Lender Certification."

## B. MODIFYING THE SBA TERMS AND CONDITIONS

1. The CDC must request in writing SBA's approval of modifications to the terms and conditions of the 504 loan at any time after approval but before funding:

   a. For an increase or decrease in the amount of an approved loan, the 327 action must clearly support the need for the change in the amount and address the effects

on repayment ability, collateral and jobs created or retained. The 327 action must also provide the revised breakdown of the private sector lender, debenture, and Applicant's injection, including a revised use of funds.

b. Any adjustments to or changes in ownership of the Borrower, including percentage of ownership. CDCs may not unilaterally approve such adjustments or changes.

2. CDCs may use their unilateral authority to submit the following 327 actions using the 504 SBA Loan System:

   a. 504 Loan Cancellation (prior to closing);

   b. Borrower, EPC or OC mailing address. Note: CDCs must not exercise unilateral authority to change the address of the Project Property;

   c. Borrower, EPC or OC phone numbers and email addresses; and

   d. Principal or guarantor mailing address, phone number, and email address.

3. For loans approved under ALP Express delegated authority, ALP CDCs are authorized to perform the servicing actions listed below. The ALP CDC is responsible for making these loan modifications (also known as 327 Actions) in the SBA Loan System for ALP Express Loans:

4. An ALP CDC may correct an error in the street address of a property pledged as collateral for the ALP Express Loan. The ALP CDC may not change the location of the Project Property using ALP Express delegated authority.

5. An ALP CDC may change a Third Party Lender or Interim Lender for an ALP Express Loan provided that the lender is a financial institution that is regulated by the Federal Financial Institution Regulators (i.e., the Federal Deposit Insurance Corporation, the Federal Reserve Board, the Office of the Comptroller of the Currency, the National Credit Union Administration, and the Farm Credit Administration) or by a state financial institution regulator with supervisory and examination authority satisfactory to SBA.

6. An ALP CDC may add inadvertently omitted co-Borrowers (without changing the ownership) and guarantors for ALP Express Loans.

7. An ALP CDC may reduce the amount of standby debt for ALP Express loans before 504 loan closing.

   a. An ALP CDC may make de minimis increases to Use of Proceeds amounts on an ALP Express Loan provided the Total Project Costs do not increase. A de minimis increase is one in which the increase to all Use of Proceeds categories does not exceed 10% of the total project cost. ALP CDCs may reduce the project size under ALP Express delegated authority with no limitations. However, if these changes necessitate modification or deletion of collateral that was originally approved, the entire action must be submitted to SLPC for prior review and

approval.

8. For loans approved under PCLP authority:
    a. Generally, PCLP CDCs may modify and extend the SBA Terms and Conditions up to 48 months from the date of approval using their unilateral authority. PCLP CDCs must upload the final modified executed terms and conditions to the SBA Loan System within 15 business days after debenture funding.
    b. PCLP CDCs must obtain prior written consent from the SLPC for any adjustments to or changes in ownership of the Borrower, including percentage of ownership, after loan approval. The SLPC will approve the proposed modification and enter it into the SBA Loan System after:
        i. Verification that the proposed changes to the ownership of the Borrower comply with limitations on the aggregate amount of SBA portions of all loans to a Borrower, including affiliates; and
        ii. Verification that there has been no prior loss to the Government caused by the new owner(s) or any business owned, operated, or controlled by the new owner(s).
    c. PCLP CDCs must obtain approval for increases or decreases in the loan amount directly in the SBA Loan System. Approval of the requested increase or decrease in the SBA Loan System will constitute SBA's prior written consent.
9. Post-approval modifications (327 actions) must be submitted to the SLPC through the 504 SBA Loan System. Detailed guidance on the 504 SBA Loan System submission process is available on the SBA website in the 504 User Guide for submitting loan applications.
10. Neither the amount nor the maturity of a loan can be modified after the debenture closing has been completed.

## C. CLOSING, DISBURSEMENT, AND POST-CLOSING

1. Interim Financing
    a. A construction escrow account may be used with SBA's prior approval if acquisition of machinery and equipment or other portions of a project (such as a parking lot, landscaping, etc.) represents a relatively minor portion of the total project, and it has been contracted for delivery at a specified price and date, but cannot be installed or delivered prior to acquisition or completion of the plant, the debenture may be sold, provided (see Paragraph A.8, Construction Loan Provisions, of this Chapter):
        i. The proceeds authorized for acquisition of such assets are held in escrow by the CSA, Title Company, CDC attorney, or bank to complete Project components;

ii. All required lien positions and collateral are obtained prior to closing;

iii. Disbursement from such account(s) must be approved by the CDC and SBA, supported by invoices, and be made payable jointly to the small business and the designated contractor; and

iv. Funds not disbursed after 1 year will be applied to pay down the Third Party Lender's loan.

The interim financing must be fully disbursed and the project completed prior to the sale of the Debenture with one exception. A portion of the debenture proceeds may be put into an escrow account to complete a minor portion of the total project (see 13 CFR § 120.961).

b. The Interim Lender must make a number of certifications at the time of the debenture closing. The certifications are stated in SBA Form 2288 and 13 CFR §§ 120.891 and 120.892. If the Interim Lender cannot certify as required, then the debenture cannot be funded.

2. Responsibility for Closing the 504 Loan and Debenture

a. The CDC is responsible for the 504 loan closing, including compliance with all SBA Loan Program Requirements. Each CDC has its own division of labor and dictates the CDC Counsel's role. Although SBA counsel is available for advice and assistance, the CDC and its attorney are ultimately responsible for the 504 Loan closing. (13 CFR §§ 120.960 and 120.10)

b. The debenture closing is the joint responsibility of the CDC and SBA. CDC must prepare the documents necessary for closing the debenture. SBA counsel reviews the loan closing package for legal sufficiency and opines whether SBA may guarantee the debenture. (13 CFR § 120.960)

c. All CDC Counsel (including Designated Attorneys and those without Designated status) who submit 504 Loan closing packages to SBA must use the form Opinion of CDC Counsel. The Opinion of CDC Counsel requires the CDC Counsel to acknowledge that SBA will rely upon the Opinion in guaranteeing the Debenture. Additionally, the Opinion requires the CDC Counsel to certify that the CDC Counsel is a licensed, active member, in good standing, of the Bar of the applicable state. If closing deficiencies that cause a loss on the 504 loan occur, SBA may pursue a claim against the CDC Counsel for the closing deficiencies. SBA will also expect the CDC to timely pursue any claims the CDC may have against the CDC Counsel as a result of closing deficiencies. Additionally, all CDC Counsel are considered to be Agents who conduct business with SBA under 13 CFR § 103.1(a). The regulation at 13 CFR § 103.4 provides that SBA may suspend or revoke an Agent's privilege to conduct business with SBA for good cause, including violations of ethical guidelines which govern the profession or business of the Agent or which are published at any time by SBA. Finally, as set

forth in Paragraph C.5.h., Withdrawal of Designated Attorney Status below, good cause for withdrawal of Designated Attorney status includes, among other things, submission of unsatisfactory 504 closing packages.

d. Priority CDCs may not use in-house counsel as its designated attorney. Because the opinion of counsel is only one component of the loan closing, a CDC may not use its in-house counsel to close a 504 loan and obtain an opinion of counsel from an outside designated attorney. The very limited circumstances under which one attorney performs the closing and another attorney provides the opinion of counsel are outlined in the boilerplate opinion of counsel and involve a project in one state and the CDC counsel in another.

3. The Closing Package

a. Types of Loan Closing Packages:

i. Regular closing package submitted by either non-Priority CDCs or Priority CDCs who are not using a Designated Attorney; and

ii. Expedited closing package submitted by a Priority CDC using a Designated Attorney under the expedited closing process.

b. The Closing Package:

i. CDCs and SBA must use SBA Form 2286, "504 Debenture Closing Checklist," (Checklist) for all 504 debenture closings. The Checklist lists the documents SBA requires to determine whether the debenture can be sold to fund the loan. It is not intended to include all the items the CDC will need to properly close the loan.

ii. SBA requires that the CDC submit to SBA counsel for review a completed SBA Form 2286 along with the required items on the Checklist. In rare circumstances if an additional document is necessary, the CDC may submit it along with an explanation of the significance.

c. Mandatory Forms:

i. Documents on the Checklist that have an SBA form number

ii. Opinion of CDC Counsel; and

iii. The SBA-approved environmental indemnification agreement.

CDCs may use their own forms for the lien instruments on Project Property and secondary collateral. Those forms must be either state bar-approved forms or approved by SBA counsel prior to submission. The lien instruments on real estate must contain a due-on-sale clause.

d. The closing process for ALP Express Loans is the same as the closing process for PCLP Loans. ALP Express Loans may only be closed using a Designated

Attorney in good standing who will execute the required Opinion of CDC counsel indicating that the project loan has been closed in accordance with the SBA Terms and Conditions of the 504 loan and SBA Loan Program Requirements for each loan. An ALP CDC must submit an ALP Express Loan closing package using a Designated Attorney under the expedited closing process described in this paragraph. In addition to the items above, the ALP CDC must also submit to SBA counsel all loan modification actions (327 Actions) on the ALP Express Loan, including those authorized under the CDC's ALP Express delegated authority as outlined in paragraph B.3 of this Chapter. ALP CDCs may not use ALP Express authority to close or service a loan that was not approved using ALP Express delegated authority but must instead process closing and servicing actions through the process that applies to the CDC's non-delegated loans.

4. Designated Attorney

   13 CFR § 120.802

   A Designated Attorney is the CDC closing attorney that SBA has approved to close loans under an expedited closing process for a Priority CDC.

   a. To become a Designated Attorney, an attorney must submit evidence of:

      i. A degree from a recognized law school;

      ii. Membership in the bar of the state in which the attorney's 504 closing practice is or will be primarily located;

      iii. Professional malpractice insurance coverage:

         a) With limits of at least $1,000,000/$1,000,000; and

         b) A deductible not to exceed $20,000 for individuals and firms with 3 or fewer attorneys, $50,000 for law firms with more than 3 attorneys or $100,000 for large law firms with more than 25 attorneys.

         c) Applicants may request from the General Counsel, or designee, an increase in the deductible or a hardship exemption with respect to the policy limits. Policy limit reductions to $500,000/$1,000,000 will only be granted to sole practitioners and small firms of three or fewer attorneys, while deductible requirement waivers will only be granted to larger firms with a demonstrated, strong financial history. The General Counsel, or designee, will consider a number of factors when deciding whether to grant or renew a hardship waiver, including, but not limited to, the documentation provided in support of the waiver request, the number of 504 loan closings by the Designated Attorney in the prior 12 months, the total dollar amount of the 504 loans closed by the Designated Attorney in the prior 12 months, and the overall quality of the loan closing packages received from the Designated Attorney. If

approved, a hardship waiver will have a duration of 1 year. If an attorney obtains designated status, renewals of hardship waivers may be sought annually for as long as the hardship exists. Approval and renewal of hardship waivers are within the discretion of the General Counsel (or designee).

d) Sole practitioners seeking a hardship waiver must state what their present annual premium is and what it would cost to get $1,000,000/$1,000,000 with $20,000 deductible and $500,000/$1,000,000 with $20,000 deductible. All other relevant financial information should also be provided.

iv. Attendance at an SBA approved 504 loan closing training course. Attorneys may fulfill this requirement up to 1 year prior to designation or within 6 months after designation; and

v. Adequate expertise in 504 loan closings.

b. Process to request Designated Attorney status:

i. The CDC nominates the attorney by submitting an application to Lead District Office in which the attorney's practice is primarily located. An application must include:

a) A submission on the attorney's letterhead addressing each of the conditions in the previous paragraph;

b) A copy of the attorney's malpractice insurance policy, or a certificate of insurance or declarations page showing the:

i) Amount of coverage and deductible;

ii) Premium; and

iii) Name of the attorney insured.

c) If the attorney requests a hardship exemption with respect to the insurance policy limits or a waiver of the amount of the deductible, the attorney must include the request with the application, supported by appropriate information, including:

i) The amount of their policy limits or deductible; and

ii) The current premium;

iii) The quote obtained for the increased premium to meet SBA's minimum professional malpractice insurance requirements (absent a hardship waiver);

iv) The size of the firm;

v) The firm's arrangement for covering the deductible, such as a loss reserve or escrow;

vi) Evidence of the firm's history and financial strength; and

vii) For sole practitioners or law firms with fewer than three attorneys, personal financial statements for each attorney seeking Designated Attorney status.

c. Other Restrictions/Requirements:

i. A designated attorney cannot be:

a) An employee of the CDC or of an Associate of the CDC; or

b) On the board of the CDC, participate in its lending decisions, or otherwise be too closely associated with the CDC, as determined by SBA counsel.

ii. An attorney may be a member of the CDC, but not an officer, provided SBA counsel determines the attorney is not too closely associated with the CDC. SBA counsel must consider the attorney's relationship with the CDC including:

a) The degree of control exerted by the attorney on the CDC's decision-making;

b) Any benefits accruing to the attorney through the attorney's association with the CDC; and

c) Any appearance of conflict of interest.

d. The Lead District Office forwards the application to the Office of General Counsel (OGC) with the recommendations of the District Director, District Counsel and other SBA District Offices, if applicable.

e. OGC will notify the attorney in writing of acceptance by SBA as a designated 504 closing attorney.

f. The Lead District Office must allow a CDC to use a non-designated attorney for a reasonable time to develop an additional designated attorney or to replace a designated attorney. In either event, SBA counsel will accept the closing package from a non-designated attorney and conduct a non-priority closing review.

g. To maintain Designated Attorney status, an attorney must:

i. Deliver annually to the 504 Loan Program Division on or before the renewal of the current policy:

a) A certificate from its insurance carrier confirming the existence of professional malpractice insurance in the amount identified in

Subparagraph a. iii above. If seeking a hardship waiver or a renewal of an existing hardship waiver, the Designated Attorney must provide:

i) The current amount of their policy limits or deductible;

ii) The current premium;

iii) The quote obtained for the increased premium to meet SBA's minimum professional malpractice insurance requirements (absent a hardship waiver);

iv) The size of the firm;

v) The firm's arrangement for covering the deductible, such as a loss reserve or escrow;

vi) Evidence of the firm's history and financial strength; and

vii) For sole practitioners or law firms with fewer than three attorneys, personal financial statements for each attorney seeking designated status.

b) Evidence of continued membership and good standing in the bar(s) of all states in which the attorney is approved to serve as designated counsel.

ii. Notify SBA immediately if there is a change of status (e.g., new address, new law firm or change in malpractice coverage); and

iii. Submit evidence of attendance at an SBA-approved closing update course every 2 years. The attorney may take the course any time within the calendar year that their status would expire to maintain their status.

h. Withdrawal of Designated Attorney status:

The General Counsel, or designee, may withdraw an attorney's Designated status for good cause, including, but not limited to: unprofessional or unethical conduct; failure to maintain the required insurance coverage; failure to attend the required training; submission of unsatisfactory 504 closing packages (based upon reviews or other evidence); failure to maintain a good working relationship and good communication with SBA; failure to maintain membership and good standing in the bar(s) of all states in which the attorney is approved to serve as designated counsel; and/or failure to comply materially with an SBA Loan Program Requirement.

5. Closing and Post-Closing Activities

**a. CDC's Responsibilities**

The CDC must:

i. Certify that the Project costs were paid in full and that the Project proceeds were used in accordance with the requirements of the SBA Terms and Conditions, and that each party to the Project contributed the required amount to the costs. To support this certification, the CDC must have evidence of the use of proceeds and the contributions by each party (Third Party Lender, Interim Lender, and Borrower). Sufficient evidence is:

a) For the purchase of land and/or building, a signed or certified Settlement Statement, or its equivalent, showing the amounts paid and whether paid by the Borrower or from the Third Party Lender or Interim Lender's loan proceeds.

b) For construction or renovations,

i) Copy of construction contract and all change orders;

ii) Evidence of each progress payment and final payment of project reflecting cumulative costs and source of payment (Third Party Lender, Interim Lender, or Borrower);

iii) If a construction escrow account is used as set forth in this SOP, copies of paid invoices and a copy of the cancelled check made payable to the Borrower and the designated contractor; and

iv) Copy of Mechanic's Lien Releases, if applicable.

c) For debt refinancing, a copy of the transcript of account and settlement statement.

d) For all other costs, a settlement statement or copies of the paid invoices and cancelled checks or evidence of wire transfers.

e) No funds should be paid directly to the Borrower unless the CDC obtains evidence of the Borrower's payments (cancelled checks and paid invoices). For 504 debt refinance balances, the principal balance of the loan(s) approved for the debt refinance may decrease between the original approved amount and the actual balance due at 504 loan closing and funding because of intervening payments made by the Borrower. SBA requires that the CDC document its file to account for the changes to the principal balance of the refinanced debt that arise after loan approval, and provide this information to District Counsel with the closing package. OCRM will include this as part of a CDCs review.

Submissions of 327 loan modification requests to SLPC are not required to reduce the originally approved debt refinance amount (with or without expansion) when:

i) Account for the principal reductions from payments made by the borrower on the debt being refinanced during the period between submission and disbursement;

ii) The principal amount of these debt payments may be reimbursed to the borrower from the proceeds of SBA-approved interim financing, or from the SBA debenture if no interim financing is used.

Submissions of 327 loan modification requests to SLPC are required when the approved project costs are reallocated, unless it is an ALP Express Loan, in which case de minimis reallocations are allowed as stated under Section C, Chapter 2, Paragraph B.3.e.

ii. Notify SBA counsel in writing of planned debenture closings at least 30 days before the SBA District Office deadline for CDCs to submit closing packages. This notification is for SBA counsel's planning purposes only and the CDC may ultimately submit more, fewer or different closing packages.

iii. Request from the SLPC all necessary modifications to the SBA Terms and Conditions before submitting closing packages as far in advance of submitting the loan closing package as possible. The CDC must obtain SBA approval of all such issues before submitting the closing package to the SBA District Office.

iv. Each CDC must issue a written opinion based upon financial statements current within 120 calendar days from the published Central Servicing Agent (CSA) Cut-Off Date for the applicable Debenture Funding Date that to the best of its knowledge there has been no unremedied substantial adverse change in the Applicant's (or Operating Company's) ability to repay the 504 loan since its submission of the loan application to SBA. This CDC opinion must be made within 14 business days prior to its request to SLPC to ship the file, and the CDC opinion must be supported by financial statements that are dated no earlier than 120 calendar days from the published CSA Cut-Off Date for the applicable Debenture Funding Date.

v. For all 504 loans except ALP and PCLP, CDCs must provide its finding to the SLPC along with copies of the financial statements. The SLPC either will notify the CDC of its approval or, if SBA disagrees with the CDC's determination of no unremedied substantial adverse change, the debenture will not close until SBA has been satisfied that any adverse change has been remedied. ALP and PCLP CDCs must submit the closing package to SBA

counsel and retain the finding and copies of the financial statements on which they relied in their files.

vi. If the debenture closing is not consummated in the month following the CDC's opinion of no unremedied substantial adverse change, the CDC must prepare a new opinion and follow the same process described above if the financial statement supporting the opinion will be more than 120 days old when the CDC requests the file from the SLPC for closing. For example, if a CDC's opinion of no unremedied substantial adverse change is made and approved in April, the debenture may be funded in May or June if the financial statements supporting the opinion remain no more than 120 days old at the time the request for the file is made. Otherwise, the CDC must submit a new opinion to the SLPC in the same manner noted above.

vii. Request that access to each SBA Terms and Conditions approval and all modifications be granted by the SLPC to the SBA counsel for closing in time to meet the SBA District Office's deadline for submission of loan closing packages. CDCs must not request access to the SBA Terms and Conditions and modifications unless the debenture is ready for closing and sale during the month following the request. If access has not been granted to SBA counsel by its loan closing package submission deadline, SBA counsel may hold over the package for the next month's debenture sale.

viii. Electronically submit closing packages by the deadline established by SBA counsel. No late closing packages will be accepted. SBA counsel will hold late packages over for the next month's debenture sale.

ix. Use only the 504 Debenture Closing Checklist and submit documents in the order appearing on the Checklist. In the column labeled "CDC" on the Checklist, the CDC must check off each document the CDC has included in the closing package or for documents not applicable to a particular transaction, write "NA" in the block. CDC must submit only a copy of each document and must retain the original until SBA counsel completes their review. After the debenture sale, the CDC must retain a copy of the closing package in its files and make it available to SBA upon request.

x. Hold all original loan documents until SBA gives the CDC written notification that SBA has completed its review of the closing package and approved the debenture sale. If SBA counsel determines that the loan is ready for funding, SBA counsel must notify the CDC and CSA that the debenture is ready for sale. If the SBA counsel determines that changes are needed in the closing documents, SBA must notify the CDC of such changes before the cut-off-date by which the CSA must receive documents from the CDC for the debenture sale. After the CDC makes the necessary changes and SBA has

approved the changes, SBA must notify the CDC and CSA that the debenture is ready for sale.

xi. Send by overnight mail to the CSA the necessary debenture closing documents for the debenture sale. After SBA sends the CDC notice of which debentures SBA has approved for sale, the CDC must send to the CSA by overnight mail the following debenture closing documents for each debenture to be sold:

a) SBA Form 1506, "Servicing Agent Agreement" (original);

b) SBA Form 1504, "Development Company 504 Debenture" (original);

c) SBA Form 1505, "Note (CDC/504 Loans)" (copy);

d) Authorization Agreement for Preauthorized Payment (Debit) and voided check (original);

e) IRS Form W-9, "Request for Taxpayer ID Number and Certification" (original); and

f) **Thirdparty lender participation fees** must be withheld from the CDC Processing Fee. Checks or other paper instruments are not accepted.

xii. Forward the original of all documents listed on SBA Form 2286, "504 Debenture Closing Checklist," (Checklist) (which serves as the original collateral listing) to the CLSC within 30 days after the debenture sale.

a) The CDC must forward the collateral file containing all the original documents listed on the Checklist to the CLSC. The CDC must use the Checklist as the collateral listing. The CDC must maintain the collateral file in a manner acceptable to SBA.

b) If the CDC has not yet received all original documents by 30 days after the debenture sale date, the CDC must send the documents it does have and must send additional documents along with a collateral listing upon receipt.

xiii. Ensure that all recorded interim lender documents are canceled of record (officially canceled at the place of recordation, as required by law) within 90 days after funding.

xiv. If a 504 loan is canceled after closing but before funding. Ensure that all recorded documents are canceled of record.

xv. Ensure that there is no open PIIA Review. If there is a PIIA Review pending, the CDC must ensure that the review has been fully resolved, allowing the CDC to move forward and close the loan.

**b. SBA Counsel's Responsibilities**

SBA Counsel Must:

i. Issue an annual 504 debenture closing schedule with SBA District Office deadlines for receiving closing packages. SBA counsel responsible for debenture closing in each SBA District Office must make available an annual schedule of the deadlines for receipt of both regular and expedited closing packages for each monthly debenture sale to the public and to CDCs who regularly submit closing packages to the district.

ii. Review closing packages. SBA counsel must use the standard Checklist to review the 8 documents submitted for an expedited closing and 13 documents submitted for a regular closing. If SBA counsel has concerns that SBA may be at material risk if the debenture is sold, then SBA counsel must contact the CDC and identify what information is reasonably necessary to address that concern. If the CDC is unable to provide the information or otherwise alleviate the concern, then the debenture will not be submitted for sale. In addition, SBA counsel must verify that the information the CDC entered onto the Debenture, Note, and Servicing Agent Agreement forms is accurate and complete.

iii. Notify CDCs of deficiencies. SBA counsel may reject late packages or packages that do not meet the standards for debenture sale. If the SBA counsel determines that changes are needed in the closing documents of packages approved for sale, SBA counsel must notify the CDC of such changes before the deadline upon which the CDC must mail the documents to CSA for the debenture sale. If SBA counsel rejects a package, SBA counsel must notify the CDC that SBA will not include the package in the scheduled sale and advise the CDC in writing of what the CDC needs to correct for the package to meet the standards for sale. The CDC may resubmit the package for a future sale with the required changes.

iv. If SBA counsel discovers an issue in reviewing the closing package that impacts closing of the loan, SBA counsel will advise the CDC and CDC Counsel. If the issue cannot be resolved, then SBA counsel will notify the Area Counsel of the issue, who will make a recommendation to OGC and OCA for a final decision.

v. Issue an SBA counsel closing opinion. Once SBA counsel is satisfied with the loan closing package (including that the CDC has made all necessary changes to the closing documents as identified by SBA counsel), SBA counsel must issue an opinion pursuant to 13 CFR § 120.960(c) stating that the debenture may be closed, SBA may execute its guarantee, and the debenture may be sold. The SBA counsel's Opinions should be sent to the SLPC.

vi. Notify the CDC and the CSA which loans SBA has approved for debenture funding. SBA counsel must notify the CDC and the CSA in writing as to which debentures the SBA District Office approves for funding in that month's sale.

vii. Complete File Reviews (CFRs):

SBA counsel must conduct a CFR of a random selection of all loan closings, whether those closing packages were submitted by Priority CDCs or non-Priority CDCs, to ensure program integrity. A Complete File Review consists of a review of the items listed on SBA Form 2303, Checklist for Complete File Review." The number and frequency of CFRs are at the discretion of SBA counsel, but no less than one package per 10 closing packages submitted by each CDC will be reviewed.

SBA counsel will notify the CDC when a loan has been selected for a CFR, and the CDC must promptly submit to SBA counsel the applicable items on SBA Form 2303 for that loan. SBA counsel will prepare a written report documenting the CFR and its results, and send a copy of that report to:

a) The CDC;

b) The CDC's 504 closing attorney that closed the loan;

c) The SBA counsel that reviewed and opined upon the loan closing package; and

d) The CLSC loan file.

If the CFR reveals closing deficiencies that could result in a loss to SBA, the CDC and/or its closing attorney must promptly correct the deficiencies, if possible. SBA may take other action, including an action against the CDC closing attorney. In the event of a loss, SBA may pursue an action against the CDC under 13 CFR § 120.938(b).

**c. Central Servicing Agent's (CSA) Responsibilities**

The CSA must:

i. Review debenture closing documents, package and price debenture for sale, and conduct debenture sale. The CSA notifies the CDC of any changes that need to be made or additional information to be provided before the debenture sale can occur.

ii. Complete the Servicing Agent Agreement and Note: The CSA fills in the remaining blanks on the Note and Servicing Agent Agreement, generating conformed pages, and executes the Servicing Agent Agreement.

iii. Distribute post-closing documents. The CSA will provide the following documents online:

a) The first page of the Note;

b) The Note amortization and prepayment schedules; and

c) Pages 3 and 4 of the Servicing Agent Agreement.

**d. Trustee's Responsibilities**

The Trustee will provide copies of the Debenture and the Debenture amortization and prepayment schedules to the CDC, CSA, or SBA, as directed.

6. Debenture Pools

Neither a Borrower nor an Associate of the Borrower may purchase an interest in a Debenture Pool in which the Debenture that funded its 504 loan has been placed. (13 CFR § 120.939)

7. Post-Disbursement Issues

a. A CDC may request changes on disbursed 504 loans by contacting the SBA CLSC.

i. Guidance on loan servicing is outlined in SOP 50 55, "504 Loan Servicing and Liquidation." CDCs may not unilaterally approve any adjustment to or change in the ownership of a Borrower, including a change in percentage of ownership, for 12 months after final disbursement on any loan.

ii. 13 CFR Part 120, subpart E outlines requirements under SBA loan servicing, liquidation, and debt collection litigation.

b. Prepayment:

The Borrower may prepay its 504 loan. The repurchase price of the Debenture shall be an amount equal to the outstanding principal balance of the Debenture, plus interest accrued and unpaid thereon to the repurchase date, plus a prepayment fee, known as a repurchase premium ("RP"). More information may be found at:

i. 13 CFR § 120.940 addresses prepayment of the 504 loan or debenture.

ii. SBA's SOP 50 55, contains information on prepayment or purchase of a development company loan or debenture.

iii. SBA Form 1504, "Development Company 504 Debenture," outlines the calculation of the prepayment fee.

iv. Guidehouse Inc. is the current Central Servicing Agent (CSA) for closed SBA 504 loans.

# CHAPTER 3: DEBENTURE PRICING AND FUNDING

13 CFR § 120.931

## A. DETERMINING SBA'S SHARE OF THE PROJECT COSTS

To price a debenture, you must determine SBA's share of a project's total cost. The following hypothetical project for a new business or for a Limited or Special Purpose Property will identify the amount of funds required to fund both the eligible project costs (Net Debenture) plus the administrative costs totals the Gross Debenture amount.

To illustrate, assume that total project costs (land, building and machinery and equipment and eligible soft costs) are $1,000,000. Assuming SBA will finance 35% of the project costs for 20 or 25 years, participation in project financing would be as follows:

| % | Participation | Amoun |
|---|---|---|
| 50% | Third-Party Lender | $500,000 |
| 35% | 504 Net Debenture | $350,000 |
| 15% | Small Business | $150,000 |
| | Total Project Costs | $1,000,00 |

## B. STEPS TO CALCULATE THE GROSS DEBENTURE

Use the following step by step pricing model procedures to determine the administrative costs and the Gross Debenture amount. Except for the underwriting fee and closing costs, each administrative cost is based on the amount of the Net Debenture.

For more information, see Ch. 1, Para. C.12 of this Section, Eligible Administrative Costs. Also see Section A, Ch. 4, Para. E., 504 Loan Program Fees and Use of Agents.

| | | | |
|---|---|---|---|
| 1 | Net Debenture | Determine the Net Debenture: | $350,000 |
| 2 | SBA Guaranty Fee (.5%) | multiply $350,000 by 0.005 = | $1,750 |
| 3 | Funding Fee (.25%) | multiply $350,000 by .0025 = | $875 |
| 4 | CDC Processing Fee (1.5%) | multiply $350,000 by .015 = | $5,250 |
| 5 | Eligible Closing Costs* | = | $2,500 |

| | | | |
|---|---|---|---|
| 6 | Gross Debenture Amount | To calculate the Gross Debenture, add items 1 through 5 above and divide the total by 0.996 for 20 or 25-year debentures (for 10-year debentures, this number would be 0.99625). This step adds the Underwriter's Fee to the total debenture. Round this number up to the next even thousand. | |
| | | Net Debenture Proceeds | $350,000 |
| | | SBA Guaranty Fee | $1,750 |
| | | Funding Fee | $875 |
| | | CDC Processing Fee | $5,250 |
| | | Closing Costs | $2,500 |
| | | Total | $360,375 |
| | | Divide by 0.99600 (0.99625 for 10-Year Debenture) | $360,065 |
| | | Round up to the next even thousand | $362,000 |
| | The Gross Debenture in this example is $ 362,000. | | |
| | Note: The Gross Debenture is calculated first because the Underwriter's Fee is based on the Gross Debenture, not the Net Debenture. | | |
| 7 | Underwriter's Fee | To determine the exact amount of the underwriter's fee, multiply the 20 or 25-year Gross Debenture by .004 (for 10-year debentures, this number would be .00375). | |
| | | Multiply $362,000 by .004 = | $1,448 |
| 8 | Balance to Borrower.<br>The difference between the Gross Debenture amount ($362,000.00) and the sum of Net Debenture proceeds ($350,000.00), processing and closing fees ($8,625.00), and Underwriter's fee ($1,448.00) goes to the Borrower. | | |

| | |
|---|---|
| | In this example, the Balance to Borrower is:<br>$362,000 – ($350,000 + $10,375 + $1,448) = $931. |

## C. SEPARATE PAYMENT OF THE DEBENTURE FEES

1. The CDC's Processing Fee and the closing costs are the only fees that can be paid upfront and deleted from the Gross Debenture calculations.
2. If the Borrower chooses to pay the CDC's Processing Fee upfront, the Borrower may be reimbursed for the CDC's Processing Fee from the debenture proceeds.
    a. If the Borrower is reimbursed, the CDC's Processing Fee will be included in calculating the Gross Debenture. The CDC will receive the fee as usual. The CDC then must reimburse the Borrower.
    b. If the Borrower does not want to be reimbursed for the CDC's Processing Fee from the debenture proceeds, the Gross Debenture calculation must include the CDC's Processing Fee in order to determine the correct Underwriter's Fee. Once the Underwriter's Fee is calculated, a zero is then entered on the CDC's Processing Fee line in the SBA Form 1506, and the dollar amounts are re-totaled and rounded to the next higher thousand for the new Gross Debenture amount.

## D. WHEN THE DEBENTURE IS PRICED

1. A Debenture is priced at time of application. If there are any changes in the 504 portion of the project costs between loan approval and project completion, the Debenture must be re- priced.
2. If the Borrower does not use the full amount of any contingency fund, then the Debenture may be re-priced as follows:
    a. If the amount of the unused contingency fund is 2% or less of the approved Gross Debenture amount, the difference must be refunded to the Borrower from the Gross Debenture proceeds by the CSA. No change is needed in the Debenture amount, and this does not require a loan modification request.
    b. If the amount of the unused contingency fund is greater than 2% of the approved Gross Debenture amount, the CDC must request a loan modification from the SLPC prior to closing to reduce the Net Debenture Proceeds by the amount of the unused contingency fund, and the Debenture amount is recalculated. (13 CFR § 120.930(c))

## E. FUNDING THE DEBENTURE

The 504 Debentures are normally sold and proceeds disbursed on the Wednesday after the second Sunday of each month. The Fiscal Agent normally negotiates the final rate and fees with underwriters on the Tuesday after the first Sunday of each month.

## F. DISBURSEMENT OF DEBENTURE PROCEEDS

On the scheduled sale date, the Gross Debenture proceeds, less the Underwriter's Fee, will be wired to the CSA. Upon receipt of the proceeds, the CSA must:

1. Deduct an amount sufficient to cover the following:
    a. Its initiation fee as computed and identified by SBA in the Servicing Agent Agreement, if applicable (not presently applicable); and
    b. A guaranty fee payable to SBA, as in effect at the time of loan approval.
2. Disburse the balance of the proceeds within 48 hours of receipt of funds as follows:
    a. Payoff the interim lender of the Net Debenture amount;
    b. CDC's Processing Fee; and
    c. Balance to Borrower based on the CSA's computations under the pricing model.

**APPENDICES**

## APPENDIX 1: FORMS AND RELATED SOPS

FBI Form FD-258 Applicant Fingerprint Form (FD-258)

FBI Form FD-258 Filing Instructions

FEMA Form 086-0-32 Standard Flood Hazard Determination Form

IRS Form 1098 Mortgage Interest Statement

IRS Form 4506-C IVES Request for Transcript of Tax Return (use March 2019 version for IVES)

IRS Form 8821 Tax Information Authorization

IRS Form W-9 Request for Taxpayer Identification Number and Certification

SBA Form 147 Note 7(a) Loans

SBA Form 148 Unconditional Guarantee

SBA Form 148 & 148L Instructions

SBA Form 148L Limited Guarantee

SBA Form 155 Standby Creditor's Agreement

SBA Form 159 Fee Disclosure and Compensation Agreement

SBA Form 413 Personal Financial Statement

SBA Form 722 Equal Employment Opportunity Statement

SBA Form 750 Lender's Loan Guaranty Agreement (Deferred Participation)

SBA Form 1050 Settlement Sheet (Use of Proceeds Certification)

SBA Form 1081 Statement of Personal History for Non-bank Lenders, CDCs, and Micro-Lenders

SBA Form 1086 Secondary Participation Guaranty Agreement

SBA Form 1088 Detached Assignment for U.S. Small Business Administration Loan Pool or Guaranteed Interest Certificate

SBA Form 1244 Application for Section 504 Loan

SBA Form 1246 Application for Certification as a Certified Development Company

SBA Form 1253 Certified Development Company (CDC) Annual Report Guide

SBA Form 1347 Supplemental Guaranty Agreement, Preferred Lenders Program

SBA Form 1502 Guaranty Loan Status and Remittance Form

SBA Form 1504 Development Company 504 Debenture

SBA Form 1505 Note – CDC/504 Loans

SBA Form 1506 Service Agent Agreement

SBA Form 1919 Borrower Information Form

SBA Form 2006 Loan Guaranty Agreement – Premier Certified Lenders Program (PCLP)

SBA Form 2101 CDC Certification

SBA Form 2229 Premier Certified Lenders Program Security Agreement

SBA Form 2230 Premier Certified Lenders Program Control Agreement

SBA Form 2233 Premier Certified Lenders Program (PCLP) Quarterly Loan Loss Reserve Report

SBA Form 2286 504 Debenture Closing Checklist

SBA Form 2287 Third Party Lender Agreement

SBA Form 2288 Interim Lender Certification

SBA Form 2288R Interim Lender Certification for Refinanced Loan

SBA Form 2289 Borrower and Operating Company Certification

SBA Form 2303 504 Debenture Closing Checklist for Complete File Review

SBA Form 2310 Supplemental Guaranty Agreement – Preferred Lenders Program for EWCP

SBA Form 2416 Lender Certification for Refinanced Loan

SBA Form 2424 Supplemental Loan Agreement SBA Express Program

SBA Form 2426 Supplemental Loan Agreement Export Express Program

SBA Form 2481 Historic Property Borrower Certification

SOP 50 53 Lender Supervision and Enforcement

SOP 50 55 504 Loan Servicing and Liquidation

SOP 50 56 SBA Lender Participation Requirements (Formerly Part 1 of SOP 50 10 6)

SOP 50 57 7(a) Loan Servicing and Liquidation

SOP 51 00 On-Site Lender Reviews/Examinations

USCIS Form G-845 Verification Request

USCIS Form I-327 Re-entry permit document

USCIS Form I-551 Alien Registration Card (aka Green Card)

USCIS Form I-751 Petition to Remove Conditions on Residence

USCIS Form I-797 Types and Functions

USCIS Form I-797C Notice of Action

## APPENDIX 2: ACRONYMS

| | |
|---|---|
| AAI | All Appropriate Inquiries |
| A/P | Accounts Payable |
| A/R | Accounts Receivable |
| ABA | American Bankers Association |
| ABL | Asset-Based Loan |
| ABV | Accredited in Business Valuation |
| ACH | Automated Clearing House |
| ALLR | Alternate Loan Loss Reserve Pilot Program |
| ALP | Accredited Lenders Program |
| AVA | Accredited Valuation Analyst |
| BBC | Borrowing Base Certificate |
| CAFS | Capital Access Financial System |
| CAIVRS | Credit Alert Verification Reporting System |
| CBP | Customs and Border Protection |
| CDC | Certified Development Company |
| CDFI | Community Development Financial Institution |
| CERCLA | Comprehensive Environmental Response, Compensation and Liability Act of 1980 |
| CFO | Chief Financial Officer |
| CFR | 1. Code of Federal Regulations; or<br>2. Complete File Review |
| CLCS | Centralized Loan Chron System |
| CLP | Certified Lenders Program |
| CLS | Country Limitation Schedule |
| CLSC | Commercial Loan Servicing Center |
| CPA | Certified Public Accountant |
| CRA | Community Reinvestment Act |
| CSA | Central Servicing Agent |

| | |
|---|---|
| CSP | Credential Service Provider |
| CUSO | Credit Union Service Organization |
| CVA | Certified Valuation Analyst |
| D&B | Dun and Bradstreet |
| D&O | Directors and Officers |
| DCIA | Debt Collection Improvement Act of 1996 |
| D/FA | Director of Financial Assistance |
| DFC | Denver Finance Center |
| D/ITF | Director, International Trade Finance |
| D/OCRM | Director of the Office of Credit Risk Management |
| DOD/DVA | Department of Defense/Department of Veterans Affairs |
| DOI | Department of the Interior |
| DS | Debt Service |
| DSC | Debt Service Coverage |
| DUNS | Data Universal Numbering System |
| EBITDA | Earnings Before Interest, Taxes, Depreciation, and Amortization |
| ECOA | Equal Credit Opportunity Act |
| EIN | Employer Identification Number |
| EMC | Export Management Companies |
| E&O | Errors and Omissions |
| EPA | Environmental Protection Agency |
| EPC | Eligible Passive Company |
| EQ | Environmental Questionnaire |
| ESA | Environmental Site Assessment |
| ESIGN | Electronic Signatures in Global and National Commerce |
| ESOP | Employee Stock Ownership Plan |
| ETC | Export Trading Companies |
| EWCP | Export Working Capital Program |
| EX-IM | Export-Import Bank |
| FBI | Federal Bureau of Investigations |

| | |
|---|---|
| FCC | Federal Communications Commission |
| FDD | Franchise Disclosure Document |
| FDIC | Federal Deposit Insurance Corporation |
| FEMA | Federal Emergency Management Agency |
| FFIR | Federal Financial Institution Regulator |
| FIRREA | Financial Institution Reform Recovery Enforcement Act |
| FIRS | Financial Institution Rating System |
| FTA | Fiscal Transfer Agency |
| GAAP | Generally Accepted Accounting Principles |
| GAO | Government Accountability Office |
| GPEA | Government Paperwork Elimination Act |
| GSA | General Services Administration |
| HELOC | Home Equity Line of Credit |
| IRA | Individual Retirement Account |
| IRCA | Immigration Reform and Control Act of 1986 |
| IRS | Internal Revenue Service |
| IT | International Trade |
| ITIN | Individual Tax Identification Number |
| IVES | Income Verification Express Service |
| L/LMS | Loan and Lender Monitoring System |
| LEA | Local Economic Area |
| LEED | Leadership in Energy and Environmental Design |
| LGPC | Loan Guaranty Processing Center |
| LLC | Limited Liability Company |
| LLRF | Loan Loss Reserve Fund |
| LOC | Line of Credit |
| LPA | Lender Profile Assessment |
| LPR | Lawful Permanent Resident |
| LPS | Loan Package Score |
| LRS | Lender Relations Specialist |

| | |
|---|---|
| LSP | Lender Service Provider |
| MOU | Memorandum of Understanding |
| MPA | Multi-Party Agreement |
| NAICS | North American Industry Classification System |
| NCUA | National Credit Union Administration |
| NEHRP | National Earthquake Hazards Reduction Program Recommended Provisions |
| NFIP | National Flood Insurance Program |
| NFRL | Non-Federally Regulated Lender |
| NMVCC | New Markets Venture Capital Company |
| OC | Operating Company |
| OCA | Office of Capital Access |
| OCC | Office of the Comptroller of the Currency |
| OCF | Operating Cash Flow defined as EBITDA |
| OCF/DS | Operating Cash Flow defined as EBITDA/Debt Service |
| OCRM | Office of Credit Risk Management |
| OFA | Office of Financial Assistance |
| OFPO | Office of Financial Program Operations |
| OGC | Office of General Counsel |
| OIG | Office of Inspector General |
| OIT | Office of International Trade |
| OMB | Office of Management and Budget |
| OPSM | Office of Performance and Systems Management |
| OREO | Other Real Estate Owned |
| PARRiS | PARRiS is an acronym for the specific risk areas or components that SBA reviews in the 7(a) program: Portfolio Performance; Asset Management; Regulatory Compliance; Risk Management; and Special Items |
| PCLP | Premier Certified Lenders Program |
| PFS | Personal Financial Statement |
| PII | Personally Identifiable Information |
| PIMS | Partner Information Management Systems |
| PLP | Preferred Lenders Program |

| | |
|---|---|
| POC | Point of Contact |
| QoE | Quality of Earnings |
| ROFR | Right of First Refusal |
| SAM | System for Awards Management |
| SBA | Small Business Administration |
| SBDC | Small Business Development Center |
| SBIC | Small Business Investment Company |
| SBLC | Small Business Lending Company |
| SBPS | Small Business Predictive Score |
| SCORE | Service Corp of Retired Executives |
| SFTP | Secure File Transfer Protocol |
| SHPO | State Historic Preservation Officer |
| SID | Same Institution Debt |
| SLPC | Sacramento Loan Processing Center |
| SMART | SMART is an acronym for the specific risk areas or components that SBA reviews in the 504 program: Solvency and Financial Condition; Management and Board Governance; Asset Quality and Service; Regulatory Compliance; Technical Issues and Mission |
| SOP | Standard Operating Procedures |
| SSN | Social Security Number |
| TIN | Tax Identification Number |
| TPL | Third Party Loan |
| TOP | Treasury Offset Program |
| UCC | Uniform Commercial Code |
| USCIS | United States Customs and Immigration Services |
| USDA | United States Department of Agriculture |
| USEAC | United States Export Assistance Center |
| USPAP | Uniform Standards of Professional Appraisal Practice |

# APPENDIX 3: DEFINITIONS

**7(a) Loans:** (13 CFR § 120.420(a) 7(a)) All references to 7(a) loans under this section include loans made under section 7(a) of the Small Business Act (15 U.S.C. 631 et seq.).

**7(a) Small Loans**: Are 7(a) Loans that are loans of $350,000 or less. 7(a) Small Loans **exclude:** Standard 7(a) loans, SBA Express, Export Express, CAPLines, Export Working Capital Program (EWCP), and Pilot Program loans.

**Agent**: (13 CFR § 103.1(a) 7(a) and 504) An authorized representative, including an attorney, accountant, consultant, packager, Lender Service Provider, or any other person representing an applicant or participant by conducting business with SBA.

**Applicant**: (13 CFR § 103.1 7(a) and 504) Any person, firm, concern, corporation, partnership, cooperative or other business enterprise applying for any type of assistance from SBA.

**Area of Operations**: (13 CFR § 120.802 504) The geographic area where SBA has approved a CDC's request to provide 504 Loan Program services to small businesses on a permanent basis. The minimum Area of Operations is the State in which the CDC is incorporated.

**Associate:** (13 CFR § 120.10 7(a) and 504)

1. An Associate of a Lender or CDC is:
    a. An officer, director, Key Employee, or holder of 20 percent or more of the value of the Lender's or CDC's stock or debt instruments, or an Agent (as defined above) involved in the loan process;
    b. Any entity in which one or more individuals referred to in paragraphs (1)(a) of this definition or a Close Relative of any such individual owns or controls at least 20 percent;
2. An Associate of a small business is:
    a. An officer, director, owner of more than 20 percent of the equity, or Key Employee of the small business;
    b. Any entity in which one or more individuals referred to in paragraphs (2)(a) of this definition owns or controls at least 20 percent; and
    c. Any individual or entity in control of or controlled by the small business (except a Small Business Investment Company (SBIC) licensed by SBA).
3. For purposes of this definition, the time during which an Associate relationship exists commences six months before the following dates and continues as long as the certification, participation agreement, or loan is outstanding:
    a. For a CDC, the date of certification by SBA;

b. For a Lender, the date of application for a loan guarantee on behalf of an applicant; or

c. For a small business, the date of the loan application to SBA, the CDC, the Intermediary, or the Lender.

**Borrower**: (13 CFR § 120.10 7(a) and 504) The obligor of an SBA business loan.

**Business Purchase Price:** In a change of ownership transaction, the price set by the purchase and sales agreement, less the portion of owner-occupied commercial real estate assets being acquired in the transaction. The portion of the owner-occupied commercial real estate is established by the appraised value.

**Central Servicing Agent (CSA):** (13 CFR § 120.802 504) An entity that receives and disburses funds among the various parties involved in 504 financing under a master servicing agent agreement with SBA.

**Certificate:**

1. (13 CFR § 120.600 **7(a) Loan Program Only**) The document the FTA issues representing either a beneficial fractional undivided interest in a Pool (Pool Certificate), or a fractional undivided interest in some or all of the guaranteed portion of an individual 7(a) guaranteed loan (Individual Certificate).
2. (13 CFR § 120.802 **504 Loan Program Only**) A document issued by SBA or its agent representing ownership of all or part of a Debenture Pool.

**Certified Development Company ("CDC"):** (13 CFR § 120.10 7(a) and 504) An entity authorized by SBA to deliver 504 financing to small businesses.

**Close Relative**: (13 CFR § 120.10 7(a) and 504) A spouse; a parent; or a child or sibling, or the spouse of any such person.

**Community Advantage Small Business Lending Company (CA SBLC)**: (13 CFR § 120.10 7(a)) A type of SBLC that is a nonprofit lending institution licensed and authorized by SBA to make loans pursuant to section 7(a) of the Small Business Act. Note: This includes former Community Advantage Pilot Lenders that were grandfathered in at the time Community Advantage SBLC licenses were authorized regardless of their profit or nonprofit status.

**Conduct Business with SBA** (13 CFR § 103.2(a)) means:

1. Preparing or submitting on behalf of an applicant an application for financial assistance of any kind, assistance from the Investment Division of SBA, or assistance in procurement and technical matters;
2. Preparing or processing on behalf of a lender or a participant in any of SBA's programs an application for Federal financial assistance;
3. Participating with or communicating in any way with officers or employees of SBA on an applicant's, participant's, or lender's behalf;

4. Acting as a Lender Service Provider; and
5. Such other activity as SBA reasonably shall determine.

**Current:** (13 CFR § 120.600 7(a)) No repayment from a Borrower to a Lender is over 29 days late measured from the due date of the payment on the records of the FTA's central registry (Pools) or the entity servicing the loan (individual guaranteed portion).

**Debenture:** (13 CFR § 120.802 504) An obligation issued by a CDC and guaranteed 100 percent by SBA, the proceeds of which are used to fund a 504 loan.

**Debenture Pool:** (13 CFR § 120.802 504) An aggregation of Debentures.

**Designated Attorney:** (13 CFR § 120.802 504) The CDC closing attorney that SBA has approved to close loans under an expedited closing process for a Priority CDC.

**Domestic-to-Foreign Export:** (7(a)) A transaction in which the Borrower sells to a foreign buyer. This definition also includes digital, service, and other intangible transactions in which no physical goods are being shipped.

**Eligible Passive Company**: (13 CFR § 120.10 7(a) and 504) A small entity or trust which does not engage in regular and continuous business activity, which leases real or personal property to an Operating Company for use in the Operating Company's business, and which complies with the conditions set forth in §120.111.

**Export Finance Manager**: (7(a)) This is the current term for the SBA employee who works at the United States Export Assistance Center.

**Export Transaction**: (7(a)) The production and payment associated with a sale of goods or services to a foreign buyer. Eligible transactions include Domestic-to-Foreign Exports, Foreign-to-Foreign Exports, and Indirect Exports.

**Exporter**: (7(a)) A small business concern engaged in or proposing to engage in an eligible Export Transaction.

**Foreign-to-Foreign Export:** (7(a)) A transaction in which the Borrower sells to a foreign buyer, but the goods do not leave a United States port of export. In Foreign-to-Foreign Export transactions, related inventory is ineligible.

**FTA:** (13 CFR § 120.600 7(a)) SBA's fiscal and transfer agent.

**Good Standing:** (13 CFR § 120.420 7(a)) In general, a Lender is in "good standing" with SBA if it:

1. Is in compliance with all applicable:
    a. Laws and regulations;
    b. Policies; and
    c. Procedures;
2. Is in good financial condition as determined by SBA;

3. Is not under investigation or indictment for, or has not been convicted of, or had a judgment entered against it for felony or fraud, or charges relating to a breach of trust or violation of a law or regulation protecting the integrity of business transactions or relationships, unless the Lender Oversight Committee has determined that good standing exists despite the existence of such factors.
4. Does not have any officer or employee who has been under investigation or indictment for, or has been convicted of or had a judgment entered against him for, a felony or fraud, or charges relating to a breach of trust or violation of a law or regulation protecting the integrity of business transactions or relationships, unless the Lender Oversight Committee has determined that good standing exists despite the existence of such person.

**Gross Debenture**: (504) Net Debenture Proceeds plus the eligible administrative costs.

**Household member:** (13 CFR § 105.201 7(a) and 504) Spouse and minor children of an employee, all blood relations of the employee and any spouse who resides in the same place of abode with the employee.

**In Margin:** when loan availability established per loan program requirements is equal to or greater than the principal balance.

**Indirect Export**: (7(a) and 504) The term "indirect export" applies to situations where, although the Borrower's direct customer is located in the United States, that customer will be exporting the items/services it purchased from the Borrower to a foreign Buyer. In such cases, the Borrower must provide documentation to the Lender from the Borrower's domestic customer (typically in the form of a letter, invoice, order, or contract) that the goods or services are in fact being exported.

**Ineligible Person:** An Ineligible Person includes, but is not limited to:

1. Undocumented aliens who are in the U.S. illegally;
2. An individual granted asylum, a refugee, a visa holder, a non-immigrant alien under 8 U.S.C. § 1101(a)(15), or those under Deferred Action for Childhood Arrivals (DACA);
3. An individual, including a visa holder, who is not a U.S. Citizen, or U.S. National (non-resident aliens);
4. An individual (including U.S. Citizens and U.S. Nationals) who has their Principal Residence outside of the United States, its territories, or possessions;
5. A business concern or entity that was created, organized, or incorporated outside of the United States, its territories, or possessions;
6. An individual who is a citizen of the People's Republic of China, or the Special Administrative Region of Hong Kong;
7. A Lawful Permanent Resident (LPRs) (commonly referred to as "green card holders"), including individuals with permanent (Unconditional) LPR status, and Conditional LPR status;

8. An individual, business concern, or entity on the Office of Foreign Assets Control (OFAC) sanctions list. See Paragraph J of this Chapter.

**Initial Currency Rate:** (13 CFR § 120.420 7(a)) The Initial Currency Rate Percentage (ICRP) measures the relationship between a securitizer's Initial Currency Rate and the SBA 7(a) loan portfolio Currency Rate at the time of the first securitization after April 12, 1999. The ICRP is calculated by dividing the securitizer's Currency Rate by the SBA 7(a) loan portfolio Currency Rate. SBA will calculate the securitizer's ICRP as of the end of the calendar quarter immediately prior to the first securitization completed after April 12, 1999.

**Interim Financing:** (504) is any disbursement of funds (other than the Borrower's contribution) to finance eligible project costs after the loan is approved by SBA but before the debenture is sold.

**Investor:** (13 CFR § 120.802 504) An owner of a beneficial interest in a Debenture pool.

**Job Created**: (504) A full-time equivalent (8 productive hours per day/40 productive hours per week) permanent or contracted employment created within 2 years of financing.

The Government Accountability Office's (GAO) methodology for calculating full-time equivalent employees demonstrates how to convert part-time or temporary jobs into "full-time equivalent" (FTE) jobs:

*Cumulative Hours Worked / Cumulative Hours Worked in a Full-Time Schedule = FTE*

For example: Assume that a full-time schedule for the 52-week work-year is 2,080 hours/year. An employee that works part-time 15 hours per week would qualify as 0.375 FTEs.

(15 hours X 52 weeks) / 2080 hours = 0.375

**Job Opportunity:** (13 CFR § 120.802 504) A full time (or equivalent) permanent job created within two years of receipt of 504 funds, or retained in the community because of a 504 loan.

**Job Retained**: (504) A job that otherwise would be lost to the community if the project was not done. An existing job should not be counted as a "Job Retained" unless the job is at risk of being lost if the project is not done. The CDC must be able to reasonably show that the job would be lost to the community if the project was not done.

**Key Employee (of a loan applicant/Borrower):** A person employed by the business who has the experience, qualifications, or required license to run the business, or who manages the business's day to day for owner(s), including making decisions about hiring and firing employees, handling payroll, and managing the business's finances.

**Key Employee (of an SBA Lender)**: Senior Managers, members of loan committees, and any Person (as defined in 13 CFR § 120.10) hired by the lender who has a meaningful participation in the direction of the operations, policies, or financial decisions of the lender.

**Lead District Office**:

1. For the 7(a) Loan Program: The SBA district office or branch office serving the geographic area where the Lender's principal office is located; and
2. For the 504 Loan Program: The Lead SBA Office as defined in 13 CFR § 120.802: "The SBA District Office designated by SBA as the primary liaison between SBA and a CDC and with responsibility for managing SBA's relationship with that CDC."

   Search SBA District Offices here

**Lender or 7(a) Lender:** (13 CFR § 120.10 7(a)) An institution that has executed a participation agreement with SBA under the guaranteed loan program.

**Lender Oversight Committee (LOC)**: (13 CFR § 120.10 7(a) and 504) A committee established within SBA by legislation, which meets at least quarterly, and which has the membership and duties set forth in § 48 of the Small Business Act as further outlined in delegations of authority published in the Federal Register. The LOC's duties include, but are not limited to, reviewing (in an advisory capacity) any lender oversight, portfolio risk management, or program integrity matters brought by the D/OCRM, and voting on formal enforcement act recommendations.

**Lender Service Provider**: (13 CFR § 103.1(d)) An Agent who carries out lender functions in originating, disbursing, servicing, or liquidating a specific SBA business loan or loan portfolio for compensation from the lender. SBA determines whether or not one is a "Lender Service Provider" on a loan-by-loan basis.

**Limited or Special Purpose Property:** (504) A limited-market property with a unique physical design, special construction materials, or a layout that restricts its utility to the use for which it was built.

**Loan Instruments**: (13 CFR § 120.10 7(a) and 504) The note, instruments of hypothecation, and all other agreements and documents related to a loan.

**Loan Program Requirements:** (13 CFR § 120.10 7(a) and 504) Requirements imposed upon Lenders, CDCs, or Intermediaries by statute; SBA and applicable government-wide regulations; any agreement the Lender, CDC, or Intermediary has executed with SBA; SBA SOPs; Federal Register notices; official SBA notices and forms applicable to the 7(a) Loan Program, 504 Loan Program, or Microloan Program; and the SBA Terms and Conditions, as such requirements are issued and revised by SBA from time to time. For CDCs, this term also includes requirements imposed by Debentures, as that term is defined in 13 CFR § 120.802. For Intermediaries, this term also includes requirements imposed by promissory notes, collateral documents, and grant agreements.

**Local Economic Area:** (13 CFR § 120.802 504) An area, as determined by SBA, that is in a State other than the State in which an existing CDC (or an applicant applying to become a CDC) is incorporated, is contiguous to the CDC's existing Area of Operations (or the applicant's proposed Area of Operations) of its State of incorporation, and is a part of a local trade area that is contiguous to the CDC's Area of Operations (or applicant's proposed Area of Operations) of

its State of incorporation. Examples of a local trade area would be a city that is bisected by a State line or a metropolitan statistical area that is bisected by a State line.

**Management Official**: (13 CFR § 120.10 7(a)) An officer, director, general partner, manager, employee participating in management, agent or other participant in the management of the affairs of the SBA Supervised Lender's activities under the 7(a) program.

**Multi-State CDC:** (13 CFR § 120.802 504) A CDC that is incorporated in one State and is authorized by SBA to operate as a CDC in a State contiguous to its State of incorporation beyond any contiguous Local Economic Areas.

**Net Book Value:** (7(a) and 504) An asset's original price minus depreciation and amortization.

**Net Debenture Proceeds:** (13 CFR § 120.802 504) The portion of Debenture proceeds that finance eligible Project costs (excluding administrative costs).

**Net Rate:** (13 CFR § 120.600 7(a)) The interest rate on an individual guaranteed portion of a loan in a Pool.

**New Business:** (7(a) and 504) A business that has been in operation for 2 years or less at the time the loan is approved. A business that has been in operation for more than 2 years at the time the loan is approved may be considered a New Business if it is a change of ownership that will result in new, unproven ownership/management and increased debt unrelated to business operations.

If there is a change of ownership, the CDC must review the management and level of debt in order to decide whether an additional Borrower's contribution of 5% is necessary. Operations are deemed to begin when the business begins generating revenue from its intended operations.

When an existing business starts or acquires a business that is in the same 6-digit NAICS code with identical ownership, and they are Co-Borrowers, SBA considers this to be a business expansion and not a new business.

**Nondepository Institution:** (13 CFR § 120.420 7(a)) A "nondepository institution" is a Small Business Lending Company ("SBLC") regulated by SBA or a Business and Industrial Development Company ("BIDCO") or other nondepository institution participating in SBA's 7(a) program.

**Non-controlling Minority Equity Investments:** To be considered as eligible equity, the investment may not be subject to any agreement to repay or make distributions to recover the investment prior to release of the SBA guaranty. To qualify as a Non-controlling Minority Equity Investors, the investor must have less than 20% equity in and exert no control over the operating business.

The Lender must also review and document the terms of all equity investments, including provisions that are realized upon the sale of the business, in their credit memorandum. When Equity Investments are used to meet the equity injection requirements, distributions to the investor that are not made solely for the purpose of satisfying the investor's tax obligations attributable to the business's income are prohibited until the 7(a) loan has been paid off.

Additional Equity Investments that are not used to meet the equity injection requirements, such as those providing additional liquidity, may receive standard distributions subject to any agreements of the Lender. The Lender may include covenants, such as DSC, in the loan agreement to ensure that the business has sufficient cash flow to make distributions beyond tax purposes.

**Non-Federally Regulated Lender (NFRL)**: (13 CFR § 120.10 7(a)) A business concern that is authorized by the SBA to make loans under section 7(a) and is subject to regulation by a state but whose lending activities are not regulated by a Federal Financial Institution Regulator.

**Note Rate:** (13 CFR § 120.600 7(a)) The interest rate on the Borrower's note.

**Operating Company**: (13 CFR § 120.10 7(a) and 504) An eligible small business actively involved in conducting business operations now or about to be located on real property owned by an Eligible Passive Company, or using or about to use in its business operations personal property owned by an Eligible Passive Company.

**Other Regulated SBLC**: (13 CFR § 120.10 7(a)) A Small Business Lending Company whose SBA operations receive regular safety and soundness examinations by a state banking regulator or a Federal Financial Institution Regulator, and which meets the requirements set forth in 13 CFR § 120.1511.

**Packager**: (13 CFR § 103.1(e)) An Agent who is employed and compensated by an Applicant or lender to prepare the Applicant's application for financial assistance from SBA. SBA determines whether or not one is a "Packager" on a loan-by-loan basis.

**Participant:** (13 CFR § 103.1 7(a) and 504) A person or entity that is participating in any of the financial, investment, or business development programs authorized by the Small Business Act or Small Business Investment Act of 1958.

**Person**:

1. (13 CFR § 120.10 applicable for 7(a) and 504 business loans) Any individual, corporation, partnership, association, unit of government, or legal entity, however organized.
2. (13 CFR § 105.201 applicable for 7(a) and 504 Standards of Conduct and Employee Restrictions and Responsibilities) An individual, a corporation, a company, an association, a firm, a partnership, a society, a joint stock company, or any other organization or institution.

**Pool:** (13 CFR § 120.600 7(a)) An aggregation of SBA-guaranteed portions of loans made by Lenders.

**Pool Assembler:** (13 CFR § 120.600 7(a)) A financial institution that:

1. Organizes and packages a Pool by acquiring the SBA-guaranteed portions of loans from Lenders;
2. Resells fractional interests in the Pool to Registered Holders; and

3. Directs the FTA to issue Certificates.

**Pool Rate:** (13 CFR § 120.600 7(a)) The interest rate on a Pool Certificate.

**Preference:** (13 CFR § 120.10 7(a) and 504) Any arrangement giving a Lender or a CDC a preferred position compared to SBA relating to the making, servicing, or liquidation of a business loan with respect to such things as repayment, collateral, guarantees, control, maintenance of a compensating balance, purchase of a Certificate of deposit or acceptance of a separate or companion loan, without SBA's consent.

**Principle Residence:** Principal Residence is defined by IRS Publication 523.

**Priority CDC:** (13 CFR § 120.802 504) A CDC certified to participate on a permanent basis in the 504 Loan Program (see §120.812) that SBA has approved to participate in an expedited 504 loan and Debenture closing process.

**Project:** (13 CFR § 120.802 504) The purchase or lease, and/or improvement or renovation of one or more long-term fixed assets by a small business, with 504 financing, for use in its business operations. Borrowers may finance multiple Projects simultaneously using separate 504 loans, subject to 504 Debenture limits. Note: This SOP uses the term Project for 7(a) also.

**Project Property:** (13 CFR § 120.802 504) One or more long-term fixed assets, such as land, buildings, machinery, and equipment, that are acquired or improved by a small business with a 504 transaction and for use in its business operations.

**Qualified Source:** (With respect to business valuations) 7(a):

A "qualified source" is an individual who regularly receives compensation for business valuations and is accredited by one of the following recognized organizations and is independent of the loan production function, not involved in the approval of the transaction, and must not have the appearance of a conflict of interest:

1. Accredited Senior Appraiser (ASA) accredited through the American Society of Appraisers;
2. Certified Business Appraiser (CBA) accredited through the Institute of Business Appraisers;
3. Accredited in Business Valuation (ABV) accredited through the American Institute of Certified Public Accountants;
4. Certified Valuation Analyst (CVA) accredited through the National Association of Certified Valuation Analysts; and
5. Business Certified Appraiser (BCA) accredited through the International Society of Business Appraisers.

**Quality of Earnings (QoE):** A QoE analysis is an independent financial due diligence report that examines the reliability, sustainability, and accuracy of a business's historical and projected earnings. The QoE must be performed by an independent qualified financial professional and

must be conducted for the benefit of the Lender. QoE must include a Cash Proof. For purposes of this requirement, a Cash Proof is a financial analysis that independently reconstructs cash receipts and disbursements by reconciling bank statement data to the income statement and tax return for each period under review.

**Referral Agent:** (13 CFR § 103.1(f)) A person or entity who identifies and refers an Applicant to a lender or a lender to an Applicant. The Referral Agent may be employed and compensated by either an Applicant or a lender.

**Registered Holder:** (13 CFR § 120.600 7(a)) The Certificate owner listed in FTA's records.

**Rentable Property**: (13 CFR § 120.10 7(a) and 504) The total square footage of all buildings or facilities used for business operations.

**Risk Rating**: (13 CFR § 120.10 7(a) and 504) An SBA internal composite rating assigned to individual SBA Lenders or Intermediaries that reflects the risk associated with the SBA Lender's or Intermediary's portfolio of SBA Loans. Risk Ratings currently range from one to five, with one representing the least risk and five representing the most risk and may be revised by SBA from time to time as published in the Federal Register through notice and comment.

**Rural Area**: 7(a) and 504: An area located in a county that the US Census Bureau has defined as at least 30 percent rural. The Census Bureau's urban-rural classification and the Census Bureau's County Classification Lookup Table can be found here: Urban and Rural (census.gov).

**Sales-Based Repayment Agreement:** A business funding agreement where a business receives a cash advance in exchange for a percentage of its future sales. (e.g. Point-of-Sale or Merchant Cash Advance (MCA)).

**SBA Assistance**: (13 CFR § 105.201 7(a) and 504) Financial, contractual, grant, managerial or other aid, including size determinations, section 8(a) participation, licensing, certification, and other eligibility determinations made by SBA. The term also includes an express decision to compromise or defer possible litigation or other adverse action.

**SBA Lender**: (13 CFR § 120.10 7(a) and 504) A 7(a) Lender or a CDC. This term includes SBA Supervised Lenders.

**SBA Loan**: The full amount of the 7(a) loan or the Gross Debenture amount of the 504 loan.

**SBA Loan System:** All current and future SBA designated electronic loan systems (electronic transmission). References to the "SBA Loan System" in this SOP shall be deemed to include those systems without need for further amendment if system names change.

**SBA Region**: SBA divides the United States and its territories into 10 regions numbered 1-10. SBA Regional Offices support SBA District Offices and promote economic development growth and competitiveness within their geographic areas.

**SBA Supervised Lender:** (13 CFR § 120.10 7(a)) A 7(a) Lender that is either a Small Business Lending Company or a NFRL.

**SBA's Secondary Market Program Guide:** (13 CFR § 120.600 7(a)) An issuance from SBA which describes the characteristics of Secondary Market transactions.

**SBA Terms and Conditions:** The digital loan guaranty authorization request by the Lender to SBA to authorize the Lender to make the loan with an SBA guaranty under the terms and conditions submitted in the SBA Loan System.

**Securitization:** (13 CFR § 120.420 7(a)) A "securitization" is the pooling and sale of the unguaranteed portion of SBA-guaranteed loans to a trust, special purpose vehicle, or other mechanism, and the issuance of securities backed by those loans to investors in either a private placement or public offering.

**Service Provider**: (13 CFR § 120.10 7(a) and 504) An entity that contracts with a Lender or CDC to perform management, marketing, legal or other services.

**Small Business Lending Company (SBLC):** (13 CFR § 120.10 7(a)) A nondepository lending institution that is SBA licensed and is authorized by SBA to make loans pursuant to section 7(a) of the Small Business Act and loans to Intermediaries in SBA's Microloan program. SBA accepts applications for SBLCs from time to time as published in the *Federal Register*.

**SOP**: (13 CFR § 120.10 7(a) and 504) SBA Standard Operating Procedures, as issued and revised by SBA from time to time. SOPs are publicly available on SBA's Web site at www.sba.gov/document/.

**Special Geographic Areas:** (504) include Alaska, Hawaii, State-designated Enterprise Zones, Empowerment Zones, Enterprise Communities, Opportunity Zones, and Labor Surplus Areas. (An "Opportunity Zone" is an economically distressed community that has been nominated by the State and certified by the Secretary of the U.S. Treasury as a community in which new investments, under certain conditions, may be eligible for preferential tax treatment.)

**Special Government Employee:** (13 CFR § 105.201 7(a) and 504) means an officer or employee of SBA, who is retained, appointed or employed to perform temporary duties on a full-time or intermittent basis, with or without compensation, for not to exceed 130 days during any period of 365 consecutive days.

**Standard 7(a) Loans**: Are 7(a) Loans that are greater than $350,000. Standard 7(a) Loans **exclude:** 7(a) Small, SBA Express, Export Express, CAPLines, Export Working Capital Program (EWCP), International Trade loans, and Pilot Program loans.

**Start-Up Business:** (7(a)) a business is a Start-Up Business if it has been in operation (i.e., generating revenue from intended operations) for 1 year or less;

**Supplemental Guarantor:** (7(a)) A person or entity that a Lender requires to provide a guaranty out of an abundance of caution and that is not otherwise required by SBA Loan Program Requirements to provide a guaranty. A non-owner spouse who is required to provide a limited guaranty in order to secure a lien on jointly owned personal real estate is not a Supplemental Guarantor, because in this case the guaranty is mandatory.

**Third Party Lender:** (504) usually a financial institution that provides the Third Party Loan and typically has a first lien on the project collateral. SBA does not permit the CDC to be the Third Party Lender on Projects financed by the CDC.

**Third Party Loan:** (13 CFR § 120.802 504) A loan from a commercial or private lender, investor, or Federal (non-SBA), State or local government source that is part of the Project financing.

**Underwriter:** (13 CFR § 120.802 504) An entity approved by SBA to form Debenture Pools and arrange for the sale of Certificates

**Veteran:** (7(a) and 504) (Title 38, Section 101(2), (10), & (18) 7(a) and 504): A person who served in the active military, naval, or air service (i.e., the United States Army, Navy, Marine Corps, Air Force, and Coast Guard, including the reserve components thereof), and who was discharged or released therefrom under conditions other than dishonorable. The term "discharge or release" includes (A) retirement from the active military, naval, or air service, and (B) the satisfactory completion of the period of active military, naval, or air service for which a person was obligated at the time of entry into such service, or, in the case of a person who, due to enlistment or reenlistment, was not awarded a discharge or release from such period of service at the time of such completion thereof and who, at such time, would otherwise have been eligible for the award of a discharge or release under conditions other than dishonorable. Further, section 3(q) of the Small Business Act defines "owned and controlled by a veteran" as a business in which one or more veterans own at least 51 percent of the business, or, in the case of a corporation, at least 51 percent of the stock, and in which one or more veterans also control the management and daily business operations.

## APPENDIX 4: DEFINITIONS – ENVIRONMENTAL

For purposes of the environmental portions of this SOP, the following definitions apply. Terms that are not defined below but are defined in CERCLA, 13 CFR or 40 CFR shall have the meaning provided in CERCLA, 13 CFR or 40 CFR.

**"Acquisition"** or **"Acquisition Date"** means the date on which a Person (as defined in this appendix) acquires title to the Property.

**"Adjoining Properties"** means any real property or properties the border of which is (are) shared in part or in whole with that of the Property, or that would be shared in part or in whole with that of the Property but for a street, road, or other public thoroughfare separating the properties (See 40 CFR § 312.20).

**"All Appropriate Inquiries" (AAI)** means the standards and practices set forth in 40 CFR § 312.20.

**"ASTM"** refers to ASTM International. www.astm.org

**"At,"** whether capitalized or not, when used with respect to the Property or Adjoining Properties, means "at, on, in, into, under, above, from or about."

**"CERCLA"** means the Comprehensive Environmental Response, Compensation and Liability Act of 1980, 42 U.S.C. § 9601 et seq.

**"Child-Occupied Facility"** means a building, or portion of a building, constructed prior to 1978, visited regularly by the same child, under 6 years of age, on at least two different days within any week (Sunday through Saturday period), provided that each day's visit lasts at least 3 hours and the combined weekly visits last at least 6 hours, and the combined annual visits last at least 60 hours. Child-occupied facilities may include, but are not limited to, day care centers, preschools, and kindergarten classrooms. Child-occupied facilities may be located in target housing or in public or commercial buildings. With respect to common areas in public or commercial buildings that contain child-occupied facilities, the child-occupied facility encompasses only those common areas that are routinely used by children under age 6, such as restrooms and cafeterias. Common areas that children under age 6 only pass through, such as hallways, stairways, and garages are not included. In addition, with respect to exteriors of public or commercial buildings that contain child-occupied facilities, the child-occupied facility encompasses only the exterior sides of the building that are immediately adjacent to the child-occupied facility or the common areas routinely used by children under age 6. See 40 CFR § 745.83.

**"Contamination"** means the presence of any Hazardous Substance at or affecting the Property, including any Hazardous Substances that have migrated to or from the Property, in such

quantities or under such conditions as to render the Property or the operations conducted thereon subject to, or potentially subject to, a directive or order from a Governmental Entity.

**"Engineering Control"** means a device or structure constructed at the Property to prevent people from coming into contact with Contamination or to prevent mobile Contamination such as groundwater Contamination from moving off site. Examples include asphalt or concrete caps, fences, extraction wells, trenches, and subsurface barrier walls.

**"Environmental Investigation"** refers to the process of assessing the environmental conditions at a Property. For example, an Environmental Investigation may include one or more of the following: an Environmental Questionnaire, Records Search with Risk Assessment, Transaction Screen Analysis, Phase I Environmental Site Assessment (Phase I ESA) or Phase II Environmental Site Assessment (Phase II ESA).

**"Environmental Investigation Report"** (or the **"Report"**) means the written account of the Environmental Investigation of the Property prepared by the Person (as defined in this appendix) who conducted the Environmental Investigation.

**"Environmental Laws"** means any and all applicable federal, state, tribal and local statutes, laws, rules, regulations, ordinances, codes, judicial or administrative orders, consent decrees, judgments, or other binding determinations of any judicial or regulatory authority, now or hereafter in effect, imposing liability, establishing standards or otherwise relating to protection of the environment, health and safety.

**"Environmental Professional"** means a person who meets the requirements set forth in 40 CFR § 312.10(b). The All Appropriate Inquiries standards defines an Environmental Professional as "a person who possesses sufficient specific education, training, and experience necessary to exercise professional judgment to develop opinions and conclusions regarding conditions indicative of releases or threatened releases…on, at, in, or to a property, sufficient to meet the objectives and performance factors [of the rule]." 40 CFR § 312.10(b). An Environmental Professional must:

1. Hold a current Professional Engineer's or Professional Geologist's license or registration from a state, tribe, or U.S. territory (or the Commonwealth of Puerto Rico) and have the equivalent of 3 years of full-time relevant experience; or

2. Be licensed or certified by the Federal government, a state, tribe, or U.S. territory (or the Commonwealth of Puerto Rico) to perform environmental inquiries as defined in § 312.21 and have the equivalent of 3 years of full-time relevant experience; or

3. Have a Baccalaureate or higher degree from an accredited institution of higher education in a discipline of engineering or science and the equivalent of 5 years of full-time relevant experience; or

4. Have the equivalent of 10 years of full-time relevant experience.

Further, SBA requires that an Environmental Professional be impartial and maintain a minimum coverage of one million dollars per claim (or occurrence) in errors and omissions insurance.

**"Environmental Questionnaire"** means the questionnaire used by a Lender to determine the likelihood that Contamination may be present at Property offered to secure an SBA-guaranteed loan. Environmental Questionnaires must be completed or reviewed by a Lender that has made at least one site visit to the Property and a good faith effort to conduct an interview with the current owner or operator of the Property. An Environmental Professional may, but is not required to, assist with the responses to the questionnaire. An Environmental Questionnaire must be dated within one year of the date of issuance of the SBA loan number. The current owner or operator of the Property must sign the Environmental Questionnaire. If the current owner or operator of the Property will not sign the Environmental Questionnaire it cannot be used and lender must then, at a minimum, obtain a Transaction Screen.

An acceptable Environmental Questionnaire must include, in addition to the required areas of inquiry listed below, the following language with respect to false statements: "The undersigned owner(s) and/or operator(s) acknowledge(s) and agree(s) that intentionally falsifying or concealing any material fact with regard to the subject matter of this Environmental Questionnaire may, in addition to other penalties, result in prosecution under applicable law including 18 U.S.C. § 1001."

Prudent lending practices dictate that an Environmental Questionnaire must include the address of the property and, at a minimum, inquire into the following areas:

- Past and present uses of the Property and Adjoining Properties, with particular attention paid to those uses by environmentally sensitive industries;
- Past and present identification of any Hazardous Substances at the Property and Adjoining Properties;
- Storage, generation, treatment, emission or disposal of Hazardous Substances at the Property and Adjoining Properties;
- Possession of permits to use, store, generate, treat, emit, or dispose of Hazardous Substances by businesses operating at the Property and Adjoining Properties;
- Evidence of Contamination at the Property and Adjoining Properties;

- Potential sources of Contamination[1] at the Property and Adjoining Properties;
- Knowledge on the part of the Borrower, seller, or Lender of any past evidence of Contamination or sources of Contamination at the Property and Adjoining Properties;
- Knowledge on the part of the Borrower, seller, or Lender of any past, threatened or pending lawsuits or administrative proceedings concerning a Release or threatened Release at the Property and Adjoining Properties;
- Existence of any regulatory actions by any Governmental Entity for environmental conditions at the Property and Adjoining Properties;
- Identification of any previously performed environmental risk studies environmental documents pertaining to the Property (attach copies); and
- Presence of lead paint, asbestos, or Polychlorinated Biphenyls ("PCBs") at the Property.

  As an alternative, SBA will accept the ASTM Questionnaire A used for Transaction Screens (currently ASTM E1528-22) for all purposes that an EQ is required by this SOP. (ASTM licenses the use of these forms, which can be obtained through www.astm.org.)

**"Good Faith"** means the absence of any intention to seek unfair advantage or to defraud another party; and honest and sincere intention to fulfill one's obligations in the conduct or transaction concerned.

**"Governmental Entity"** means any federal, state, commonwealth, tribal or local government branch, authority, district, agency, court, tribunal, department, officer, official, board, commission or other instrumentality that exercises any form of jurisdiction or authority under any Environmental Law.

**"Hazardous Substance"** means and includes any substance, material or waste regulated by CERCLA or any other Environmental Law, and specifically includes petroleum products.

**"Institutional Control"** means a legal or administrative action or requirement imposed on the Property to minimize the potential for human exposure to Contamination or to protect the integrity of Remediation. Examples include deed notices, deed restrictions, and long-term site monitoring or site security requirements.

**"Lender"** refers to banks, non-bank lenders, credit unions, certified development companies, and any other entities that participate as a lender in SBA programs. The term Lender does not include the Third Party Lender on a 504 loan.

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[1] Sources of Contamination may include, but are not limited to, the following: (1) damaged or discarded automotive or industrial batteries; (2) pesticides, paints or other chemicals stored in individual containers greater than 5 gallons in volume or 50 gallons in the aggregate; (3) chemicals in industrial drums or sacks; (4) pits, ponds or lagoons used for waste disposal or storage; (5) fill dirt from a contaminated or unknown source; (6); underground or above-ground storage tanks; (7) vent pipes, fill pipes or access ways indicating a fill pipe protruding from the ground; (8) flooring drains or walls within a facility that are stained by substances other than water and/or are emitting noxious odors; (9) clarifiers, pits or sumps; (10) dry wells

**"Multi-Unit Building"** means any non-industrial, multi-unit building that is comprised of four or more individual units.

**"Person"** means an individual, firm, corporation, limited liability company, limited liability partnership, association, partnership, consortium, joint venture, commercial entity, tribe, or trust, public, governmental, or interstate body, agency or instrumentality.

**"Phase I Environmental Site Assessment" (Phase I ESA)** means an AAI compliant Phase I ESA conducted by an Environmental Professional in accordance with the most recently adopted standard for a Phase I ESA established by ASTM International, currently ASTM E1527-21. (See also 40 CFR § 312.20.)

A person who does not qualify as an Environmental Professional may assist in the conduct of All Appropriate Inquiries if such person is under the supervision or responsible charge of a person meeting the definition of an Environmental Professional when conducting such activities, provided an Environmental Professional reviews and signs the Phase I ESA.

A Phase I ESA must contain an opinion by the Environmental Professional as to whether the inquiry has identified conditions indicative of Recognized Environmental Conditions (RECs), Controlled Recognized Environmental Conditions (CRECs), Historical Recognized Environmental Conditions (HRECs) and/or Environmental Issues at the Property. Additionally, SBA requires that all Phase I ESAs contain a conclusion by the Environmental Professional that performs the assessment that either: (1) the risk of Contamination at the Property is so minimal that no further investigation is warranted; or (2) there is risk sufficient to warrant additional investigation. Alternatively, the Environmental Professional may include a similar statement to this effect. If further investigation is warranted, the Environmental Professional should provide a detailed description of the recommendation.

The Environmental Protection Agency (EPA) sets forth time frames for the viability of Phase I ESAs (See 40 CFR § 312.20.) For SBA's purposes, and notwithstanding the EPA's regulations on updating Phase I ESAs after 180 days, SBA will accept for review an otherwise AAI compliant Phase I ESA if it is dated within one year of the date of issuance of the SBA loan number. ***Parties may still wish to strictly comply with EPA's regulatory timeframes to avoid jeopardizing legal and regulatory protections.***

Note: The immediately preceding paragraph does not apply to liquidation situations under SOP 50 55 or SOP 50 57.

**"Phase II Environmental Site Assessment" (Phase II ESA)** means an Environmental Investigation, which at a minimum, is conducted by an Environmental Professional in accordance with the most recently adopted standard for a Phase II ESA process established by ASTM International, currently ASTM E1903-19 (2020). SBA will recognize a Phase II ESA conducted in accordance with generally-accepted industry standards of practice and consisting of

a scope of work that would be considered reasonable and sufficient to identify the presence, nature, and extent of a Release.

**"Property"** means any interest in commercial real estate upon which a security interest such as a mortgage, deed of trust, or leasehold deed of trust is required as collateral for a loan or debenture.

**"Records Search with Risk Assessment"** means and includes (1) a search of the government databases identified in 40 CFR § 312.26 for an AAI compliant Phase I as well as a search of historical use sources (for example, aerial photography, city directories, reverse directories and/or fire insurance maps) pertaining to the Property and Adjoining Properties; and (2) a risk assessment by an Environmental Professional based on the results of the records search as to whether the Property is either "low risk" or "elevated risk" or "high risk" for Contamination. While the choice of standard historical sources to be reviewed on any particular site is at the discretion of the Environmental Professional in their professional judgment, the historical sources should identify property uses back to the property's first developed use, or back to 1940, whichever is earlier. The Environmental Professional need only review as many of the standard historical sources as are necessary, reasonably ascertainable, and likely to be useful. The Environmental Professional should comment upon any data failure or data gap encountered. The report must identify by name the Environmental Professional who performed the risk assessment and must include all of the database reports and historical sources relied upon. (Note that this report need not be addressed to the SBA and need not be accompanied by a Reliance Letter.) A Records Search with Risk Assessment must be dated within one year of the date of issuance of the SBA loan number.

**"Release"** means the presence of or any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, seeping, migrating, dumping or disposing of any Hazardous Substance into the environment including the abandonment or discarding of barrels, drums, tanks, and similar receptacles and containers, containing Hazardous Substances.

**"Reliance Letter"** means SBA's standard reliance letter pertaining to Environmental Investigation Reports, a copy of which is located in Appendix 5. The language in SBA's standard reliance letter may not be modified. Additionally, Lenders and CDCs should not enter into any agreement that alters the terms of SBA's standard reliance letter.

**"Remediation"** or **"Remedial Action"** and their derivatives (such as **"Remediate"**) means and includes any clean-up, corrective action or monitoring required to comply with applicable Environmental Laws including all actions within the definition of "removal" and "remedial" actions as those terms are defined in applicable Environmental Laws.

**"SBA Environmental Indemnification Agreement"** or **"SBA Indemnification Agreement"** means SBA's standard environmental indemnification agreement, a copy of which is located in

Appendix 8. The language in SBA's standard environmental indemnification agreement may not be modified.

**"Transaction Screen"** means an Environmental Investigation pursuant to the most recently adopted standard practice for limited environmental due diligence established by ASTM International, currently ASTM E1528-22. The basic elements of a Transaction Screen include: (1) an interview with the owner or operator of the Property; (2) a visit to the Property; (3) completion of both environmental questionnaires A and B, and (4) a review of government records and historical sources. Additionally, SBA requires that an Environmental Professional supervise the site reconnaissance and conclude either (a) the risk of Contamination at the site is so minimal that no further investigation is warranted; or (b) there is risk sufficient to warrant additional investigation. Alternatively, the Environmental Professional may include a similar statement to this effect. If further investigation is warranted, the Environmental Professional should provide a detailed description of the recommendation. The database records and historical records search must be attached to the Transaction Screen. A Transaction Screen must be dated within one year of the date of issuance of the SBA loan number

## APPENDIX 5: RELIANCE LETTER

**[Letterhead of Environmental Professional or Environmental Professional's Firm]**

## RELIANCE LETTER

[Date]

To: [Insert name and address of SBA Lender here] ("Lender")

and

U.S. Small Business Administration ("SBA")

Re: Borrower Name:
Project Address ("Property"):
Environmental Investigation Report Number(s):

Dear Lender and SBA:

[Name of Environmental Professional] ("Environmental Professional") meets the definition of an Environmental Professional as defined by 40 C.F.R. § 312.10(b) and has performed or supervised the performance of the following "Environmental Investigation(s)" (check all that apply):

____A Transaction Screen of the Property dated _____, 20____, and any addendum(s) thereto, conducted in accordance with ASTM International's most recent standard (currently ASTM E1528-22);

____A Phase I (or an Updated Phase I) Environmental Site Assessment of the Property dated _____, 20____, and any addendum(s) thereto, conducted in accordance with ASTM International's most recent standard (currently ASTM E1527-21). In addition, the Environmental Professional has addressed the performance of the "additional inquiries" set forth at 40 C.F.R. § 312.22;

____A Phase II Environmental Site Assessment of the Property dated _____, 20____, and any addendum(s) thereto, conducted in accordance with generally-accepted industry standards of practice and consisting of a scope of work that would be considered reasonable and sufficient to identify the presence, nature and extent of a Release as it impacts the Property.

Reliance by SBA and Lender. Environmental Professional (and Environmental Professional's firm, where applicable) understand(s) that the Property may serve as collateral for an SBA-guaranteed loan, a condition for which is an Environmental Investigation of the Property by an Environmental Professional. Environmental Professional (and Environmental Professional's firm, where applicable) authorize(s) Lender and SBA to use and rely upon the Environmental Investigation. Further, Environmental Professional (and Environmental Professional's firm, where applicable) authorize(s) Lender and SBA to release a copy of the Environmental Investigation to the Borrower for information purposes only. This letter is not an update or modification to the Environmental Investigation. Environmental Professional (and Environmental Professional's firm, where applicable) makes no representation or warranty, express or implied, that the condition of the Property on the date of this letter is the same or similar to the condition of the Property described in the Environmental Investigation.

Insurance Coverage. Environmental Professional (and/or Environmental Professional's firm, where applicable) certifies that they or the firm were covered as of the date of the Environmental Investigation by errors and omissions liability insurance with a minimum coverage of $1,000,000 per claim (or occurrence) and that evidence of this insurance is attached. As to the Lender and SBA, Environmental Professional (and Environmental Professional's firm, where applicable) specifically waive(s) any dollar amount limitations on liability up to $1,000,000 as well as any time limitations on liability, other than state or Federal statutes of limitation.

Waiver of Right to Indemnification. Environmental Professional and Environmental Professional's firm waive any right to indemnification from the Lender and SBA.

Impartiality. Environmental Professional certifies that (1) to the best of their knowledge, Environmental Professional is independent of and not a representative, nor an employee or affiliate of seller, Borrower, operating company, or any person in which seller has an ownership interest; and (2) the Environmental Professional has not been unduly influenced by any person with regard to the preparation of the Environmental Investigation or the contents thereof.

Acknowledgment. The undersigned acknowledge(s) and agree(s) that intentionally falsifying or concealing any material fact with regard to the subject matter of this letter or the Environmental Investigations may, in addition to other penalties, result in prosecution under applicable laws including 18 U.S.C. § 1001.

_____

Signature of Environmental Professional

Printed Name:

**(Note: The Environmental Professional must always sign this letter above. If the Environmental Professional is employed or retained by an Environmental Firm, then an authorized representative of the firm must also sign below).**

_____

Signature of representative of firm who is authorized to sign this letter

Printed Name & Title:

Name of Environmental Firm:

Enclosure: Evidence of Insurance

## APPENDIX 6: NAICS CODES OF ENVIRONMENTALLY SENSITIVE INDUSTRIES*

A 3 digit NAICS code includes all industries beginning with those 3 digits.

A 4 digit NAICS code includes all industries beginning with those 4 digits.

A 5 digit NAICS code includes all industries beginning with those 5 digits.

A 6 digit NAICS code includes only that industry under that industrial code.

211 OIL & GAS EXTRACTION

212 MINING (EXCEPT OIL & GAS)

213 SUPPORT ACTIVITIES FOR MINING

237 HEAVY & CIVIL ENGINEERING CONSTRUCTION

311 FOOD MANUFACTURING *(if fuel tanks present)*

312 BEVERAGE & TOBACCO PRODUCT MANUFACTURING *(except breweries, 31212)*

313 TEXTILE MILLS *(not required if sewing, weaving, or hemming only)*

314 TEXTILE PRODUCT MILLS *(not required if sewing, weaving, or hemming only)*

316 LEATHER & ALLIED PRODUCT MANUFACTURING *(not required if assembly only)*

321 WOOD PRODUCT MANUFACTURING *(if finishing occurs on site)*

322 PAPER MANUFACTURING

323 PRINTING & RELATED SUPPORT ACTIVITIES

324 PETROLEUM & COAL PRODUCTS MANUFACTURING

325 CHEMICAL MANUFACTURING

326 PLASTICS & RUBBER PRODUCTS MANUFACTURING *(not required if assembly only)*

327 NONMETALLIC MINERAL PRODUCTS MANUFACTURING

331 PRIMARY METAL MANUFACTURING

332 FABRICATED METAL PRODUCT MANUFACTURING *(not required if assembly only)*

333 MACHINERY MANUFACTURING *(not required if assembly only)*

334 COMPUTER & ELECTRONIC PRODUCT MANUFACTURING *(not required if assembly only)*

335 ELECTRICAL EQUIPMENT, APPLIANCE & COMPONENT MANUFACTURING *(not required if assembly only)*

336 TRANSPORTATION EQUIPMENT MANUFACTURING

337 FURNITURE & RELATED MANUFACTURING (*if finishing occurs on site*)

339 MISCELLANEOUS MANUFACTURING *(only required if hazardous materials are involved)*

42311 AUTOMOBILE & OTHER MOTOR VEHICLE MERCHANT WHOLESALERS *(if service bays present)*

42314 MOTOR VEHICLE PARTS (USED) MERCHANT WHOLESALERS

4235 METAL & MINERAL MERCHANT WHOLESALERS

42393 RECYCLABLE MATERIAL MERCHANT WHOLESALERS

4246 CHEMICAL & ALLIED PRODUCTS MERCHANT WHOLESALERS

4247 PETROLEUM & PETROLEUM PRODUCTS MERCHANT WHOLESALERS

441 MOTOR VEHICLE & PARTS DEALERS *(if service bays present)*

457 GASOLINE STATIONS & FUEL VENDORS *(not required for propane or firewood dealers)*

481 AIR TRANSPORTATION

482 RAIL TRANSPORTATION

484 TRUCKING *(if service bays, truck washing, or fuel tanks present)*

486 PIPELINE TRANSPORTATION

488 Support Activities for Transportation (*if fuel tanks are present or if repairs or maintenance is performed on site*)

53212 TRUCK, UTILITY TRAILER, AND RV (RECREATIONAL VEHICLE) RENTAL & LEASING *(if repairs, maintenance, or vehicle washing are performed onsite)*

53241 CONSTRUCTION, TRANSPORTATION, MINING & FORESTRY MACHINERY & EQUIPMENT RENTAL & LEASING *(if repairs, maintenance, or vehicle washing are performed onsite)*

53249 OTHER COMMERCIAL & INDUSTRIAL MACHINERY & EQUIPMENT RENTAL & LEASING *(if repairs, maintenance, or vehicle washing are performed onsite)*

54138 TESTING LABORATORIES & SERVICES

56171 EXTERMINATING & PEST CONTROL SERVICES

562 WASTE MANAGEMENT & REMEDIATION SERVICES

6221 GENERAL MEDICAL & SURGICAL HOSPITALS *(if fuel tanks are present)*

713990 OTHER RECREATIONAL INDUSTRIES *(indoor and outdoor shooting ranges only)*

71391 GOLF COURSES & COUNTRY CLUBS

71392 SKIING FACILITIES

71393 MARINAS

7212 RV (RECREATIONAL VEHICLES) PARKS & RECREATIONAL CAMPS *(if fuel tanks are present or if vehicle repairs or maintenance is performed onsite)*

8111 AUTOMOTIVE REPAIR & MAINTENANCE (*except for "car wash only" facilities, for which a Transaction Screen is an acceptable starting point*)

8112 ELECTRONIC & PRECISION EQUIPMENT REPAIR & MAINTENANCE *(not required if assembly only)*

8113 COMMERCIAL & INDUSTRIAL MACHINERY & EQUIPMENT REPAIR & MAINTENANCE

8122 DEATH CARE SERVICES *(unless no embalming or cremation at the Property)*

8123 LAUNDRY & DRY CLEANING SERVICES *(if dry cleaning operations have ever existed on site)*

812921 PHOTOFINISHING LABORATORIES *(except one hour)*

*A Phase I should always be obtained if the business sells, supplies or dispenses fuel, gasoline, heating oil, even if the NAICS code for the business is not identified on this list of environmentally sensitive industries.

A complete list of industries and corresponding NAICS codes is available.

# APPENDIX 7: REQUIREMENTS PERTAINING TO GAS STATION LOANS

## Environmental Investigation Requirements for Gas Station Loans

**NOTE: SBA Lenders are reminded that documentation associated with gas station loans can be voluminous and complex.**

The Environmental Investigation requirements set forth below apply to all loans secured by a lien or security interest on real property (a fee simple or leasehold mortgage, deed of trust, etc.*) or* personal property (gas station fixtures or equipment such as tanks, pumps, lines, etc.) currently used to operate a gas station or commercial fueling facility ("Gas Station Loans"). These requirements would not apply when the applicant operates a business, such as a convenience store associated with a gas station, in which the applicant only leases the real or personal property and neither the real nor personal property is used as collateral for the loan. Nor do these requirements apply to situations where the only collateral for the loan is something other than gas station equipment (for example, food inventory, shelving, etc.).

A. Environmental Site Assessment. The Environmental Investigation for all Gas Station Loans (including those secured by gas station equipment only) must:

   1. Begin with a Phase I ESA with the additional requirement that it be conducted by an independent Environmental Professional;
   2. Include an analysis of all relevant environmental records concerning the Property and Adjoining Properties, including any records provided by the seller if the loan is to purchase the Property;
   3. Include documentation supporting the Environmental Professional's determination of compliance with all regulatory requirements, if any, pertaining to tank and equipment testing (see Paragraph B. below) (even if the loan is secured by real property);
   4. Include the results of any further investigation, which may include a Phase II, recommended by the Environmental Professional (Any Phase II performed in connection with a Gas Station Loan must be conducted by an independent Environmental Professional *who holds a current Professional Engineer's or Professional Geologist's license and has the equivalent of 3 years of full time relevant experience*.); and
   5. If the Property is Contaminated, include a detailed description of and cost estimate for the recommended Remediation.

B. The Environmental Investigation performed by the Environmental Professional must include a determination whether the gas station is in compliance with all regulatory requirements, if any, pertaining to tank and equipment testing. A loan may not be disbursed until full compliance is achieved. Further, any leaking or otherwise defective equipment, systems, containment devices, etc., must be replaced or repaired prior to disbursement.

C. Results of Environmental Investigation.

1. Property is not Contaminated. If the Environmental Professional concludes that the Property is not Contaminated, (except on PLP, 7(a) Small Loans, SBA Express, Export Express, and PCLP loans) it is the SBA Lender's responsibility to certify in the SBA Loan System that the Property complies with all SBA environmental requirements in this SOP (which includes the additional requirements of this Appendix), and the SBA Lender must maintain the Environmental Investigation Reports(s) in the SBA Lender's loan file.

2. Property is Contaminated. If the Environmental Professional concludes that the Property is Contaminated, the SBA Lender can either:

   a. Decline the loan; or

   b. Follow the requirements in Section A, Ch. 5, Para. E.5, Property Contamination or Remediation," *provided that at a minimum, in change of ownership situations, the SBA Indemnification Agreement as described in Section A, Chapter 6, E.6.d.i, Indemnification, must always be obtained and signed by the seller*. (There may be situations where it is not practical to require the seller to sign the indemnification agreement; for example, the property is being sold from a probate estate or through a trustee in bankruptcy. Waivers may be sought from the SBA Environmental Committee at EnvironmentalAppeals@sba.gov on a case-by-case basis. A mere unwillingness on the part of a seller to execute the indemnification agreement is not a sufficient basis for a waiver. PLP, 7(a) Small, SBA Express, and Export Express Lenders and PCLP CDCs do not have the authority to grant a waiver and are also required to follow this procedure.) In addition, prudent lending practices may require an SBA Lender to utilize some of the other listed mitigating factors such as requiring additional collateral.

D. When Waiver and Release of Right to Indemnification from SBA/SBA Lender Required. If any oil company or other Person (as defined in Appendix 4) has a right to indemnification from subsequent owners of the Property (e.g., SBA/SBA Lender after acquiring Property through foreclosure or other means), then they must execute either the SBA Indemnification Agreement or another document in which they waive all known and unknown rights and release all claims and causes of action whether now or hereafter in existence against SBA and SBA Lender related to Contamination at the Property including the right to indemnification. The document containing the waiver and release must be recorded. 7(a) Lenders, except when processing a loan under delegated authority, and CDCs, including PCLP CDCs, must submit all waiver and releases to EnvironmentalReviews@sba.gov and upload these documents to the SBA Loan System, along with a copy of the title report, the document providing for indemnification, and the purchase and sale documents, if any.

# APPENDIX 8: SBA ENVIRONMENTAL INDEMNIFICATION AGREEMENT

SBA Loan No: _____

This SBA Environmental Indemnification Agreement ("Agreement") effective _____, is executed by _____ ("Borrower"), _____ [insert name(s) of indemnitor(s) not obligated on the Loan)] ("Third Party Indemnitor"), (Borrower and Third Party Indemnitor collectively referred to as "Indemnitors"), _____ [Insert name of Certified Development Company or 7(a) Lender] ("Lender") and the U.S. Small Business Administration ("SBA").

The parties to this Agreement mutually agree as follows:

## I. RECITALS

Borrower has applied for an SBA loan from Lender in the principal amount of $_____ [insert full loan amount] (the "Loan") to be evidenced by a promissory note (the "Note") and secured by a "Mortgage" encumbering certain real and personal property (collectively, the "Property") described in the "Loan Documents" including the land located at _____ [insert address] and described in Exhibit "A" attached hereto.

SBA and Lender are not willing to make the Loan without the execution and delivery of this Agreement.

## II. DEFINITIONS

For purposes of this Agreement: (1) whenever the singular form of a word is used it includes the plural, and whenever the plural form of a word is used it includes the singular; (2) the word "or" has the inclusive meaning represented by the phrase "and/or"; (3) terms used in this Agreement that are not defined below but are defined in either 13 CFR, the Comprehensive Environmental Response, Compensation and Liability Act of 1980, 42 U.S.C. §§ 9601-9875 ("CERCLA") or 40 CFR, shall have the meaning provided in 13 CFR, CERCLA or 40 CFR; and (4) unless the context otherwise clearly requires, the following definitions apply:

**A.** "**Adjoining Properties**" means any real property or properties the border of which is (are) shared in part or in whole with that of the Property, or that would be shared in part or in whole with that of the Property but for a street, road, or other public thoroughfare separating the properties.

**B.** **"At",** whether capitalized or not, when used with respect to the Property or Adjoining Properties, means "at, on, in, into, under, above, from or about."

**C.** **"Borrower"** means the Person(s) identified as the Borrower in the Loan Documents and the first paragraph of this Agreement and includes any successor in interest by virtue of assumption, merger, acquisition, transfer, assignment or otherwise.

**D.** **"Contamination"** means the presence of any Hazardous Substance at or affecting the Property, including any Hazardous Substances that have migrated to or from the Property, provided such Hazardous Substances are present in such concentrations or under such conditions as to create a violation, liability or duty to conduct a response under any Environmental Law.

**E.** **"Engineering Control"** means a device or structure constructed at the Property to prevent people from coming into contact with Contamination or to prevent mobile Contamination such as groundwater Contamination from moving off site. Examples include asphalt or concrete caps, fences, extraction wells, trenches, and subsurface barrier walls.

**F.** **"Environmental Activity"** means any use, storage, holding, existence, Release, emission, discharge, generation, processing, abatement, removal, disposition, handling or transportation of any Hazardous Substance.

**G.** **"Environmental Claim"** means any written complaint, summons, action, citation, notice of violation, directive, order, claim, litigation, investigation, judicial or administrative proceeding or action, judgment, lien, demand, letter or communication from any Person (as defined in Appendix 4) alleging non-compliance with any Environmental Law, Institutional Control or Engineering Control, relating to any actual or threatened Release, or arising from an Environmental Activity.

**H.** **Environmental Investigation"** means an investigation of the Property that: (1) is conducted by an independent Environmental Professional; (2) begins with a Phase I Site Assessment in accordance with ASTM E1527-21 that includes a review of all relevant and material environmental records concerning the Property and Adjoining Properties in the actual or constructive possession, custody or control of the Borrower including, if any, those provided by the seller; and (3) includes any other investigation recommended by the Environmental Professional conducting the Phase I to determine and document the nature and extent of any Contamination and the cost to remediate it such as record reviews, soil and water testing, or underground storage tank inspections.

**I.** **"Environmental Investigation Report"** (or the "Report") means the written account of the Environmental Investigation of the Property attached as Exhibit "B", which: (1) is signed by the Environmental Professional who conducted the Environmental Investigation; (2) includes a reliance letter that specifically grants SBA and Lender the right to rely on the

Report; and (3) includes a detailed list of all relevant and material environmental records utilized by the Environmental Professional to establish the nature and extent of Contamination including those pertaining to past or on-going Remediation at the Property or Adjoining Properties.

**J.** **"Environmental Laws"** means any and all applicable federal, state tribal and local statutes, laws, rules, regulations, ordinances, codes, principles of common law, judicial orders, administrative orders, consent decrees, judgments, permits, licenses or other binding determinations of any judicial or regulatory authority, now or hereafter in effect, imposing liability, establishing standards of conduct or otherwise relating to protection of the environment (including natural resources, surface water, groundwater, soils, and indoor and ambient air), health and safety, land use matters or the presence, use, generation, treatment, storage, disposal, Release or threatened Release, transport or handling of Hazardous Substances.

**K.** **"Environmental Professional"** means a person who meets the requirements set forth in 40 CFR § 312.10(a).

**L.** **"Governmental Entity"** means any federal, state, commonwealth, tribal or local government branch, authority, district, agency, court, tribunal, department, officer, official, board, commission or other instrumentality that exercises any form of jurisdiction or authority under any Environmental Law.

**M.** **"Hazardous Substance"** means and includes any substance, material or waste regulated by CERCLA or any other Environmental Law, and specifically includes petroleum products, radioactive materials, asbestos, polychlorinated biphenyls, and radon gas.

**N.** **"Including,"** and its derivatives such as “include” and “includes,” whether or not capitalized, means including without limitation.

**O.** **"Indemnified Parties"** means and includes SBA and Lender.

**P.** **"Institutional Control"** means a legal or administrative action or requirement imposed on the Property to minimize the potential for human exposure to Contamination or to protect the integrity of a Remedy. Examples include deed notices, deed restrictions, and long-term site monitoring or site security requirements.

**Q.** **"Lender"** means the Person identified as the Lender in the first paragraph of this Agreement and any successor in interest by virtue of merger, acquisition, transfer, assignment or otherwise including any Person acquiring the Property or the Loan from Lender or SBA.

**R.** **"Loan Documents"** means and includes the Note, the Mortgage, and any other document regarding the Loan. This Agreement is one of the Loan Documents, but it is not secured by the Mortgage.

**S.** **"Mortgage"** means the Mortgage identified in the Recitals section of this Agreement and includes all liens that secure the Loan regardless of their method of creation including those created by recording a mortgage, deed of trust, assignment of rents, collateral assignment of purchaser's interest in land sale contract or a Uniform Commercial Code financing statement. The Mortgage secures the Loan and all extensions, modifications, replacements, renewals, substitutions or consolidations thereof, including increases to the principal balance of the Note resulting from payment of expenses incurred to enforce the terms of the Note or other Loan Documents, or to preserve or dispose of the collateral securing the Loan, such as payments for property taxes, prior liens, insurance, appraisals, and attorney's fees and costs.

**T.** **"Mortgage Release Date"** means the earlier of the following two-dates: (1) the date on which the indebtedness and obligations secured by the Mortgage have been fully paid and performed and the Mortgage has been released of record; or (2) the date on which the Mortgage is foreclosed, or a conveyance by a deed in lieu of foreclosure is effective, and possession of the Property has been given to and accepted by a Person other than Lender or SBA free of occupancy, redemption rights or any other claim by Borrower or guarantors of the Loan.

**U.** **"Person"** means an individual, firm, corporation, limited liability company, limited liability partnership, association, partnership, joint venture, commercial entity, tribe, trust, or Government Entity.

**V.** **"Property"** means all or any portion of the real and personal property identified in the Recitals section of this Agreement, including all improvements, fixtures and equipment, soil, ground water, surface water, air, waterways, and water bodies associated with the real property.

**W.** **"Purchase and Sale Documents"** means and includes every document memorializing each agreement related to Borrower's acquisition of the Property including the purchase and sale agreement and amendments thereto, and all related documents such as supply agreements, deeds, environmental declarations, rights of first refusal, options, etc.

**X.** **"Release",** when used with respect to the Property or Adjoining Properties, means the presence of or any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, seeping, migrating, dumping or disposing of any Hazardous Substance into the environment including the abandonment or discarding of barrels, drums, tanks, and similar receptacles and containers, containing Hazardous Substances.

**Y.** **"Remediation"** or **"Remedial Action"** and their derivatives (such as "Remediate") means and includes any investigation, clean-up, corrective action or monitoring required to comply with applicable Environmental Laws including all actions within the definition of "removal" and "remedial" actions as those terms are defined in applicable Environmental Laws.

**Z.** **"Third Party Indemnitor"** means, individually and collectively, the Person(s) identified as the Third Party Indemnitor in the first paragraph of this Agreement and includes any successor in interest by virtue of merger, acquisition, transfer, assignment or otherwise.

## III. REPRESENTATIONS AND WARRANTIES

**A.** **Full Disclosure of Property Purchase and Sale Agreement.** If the Loan is to enable Borrower to acquire the Property, Borrower represents and warrants that all of the relevant and material terms and conditions of the purchase and sale of the Property have been disclosed to Lender and that Borrower has provided Lender with an accurate and complete copy of the Purchase and Sale Documents.

**B.** **Control of Property.** If the Loan is to enable Borrower to acquire the Property from Third Party Indemnitor, Third Party Indemnitor represents and warrants that the Property is free from all encumbrances that could enable Third Party Indemnitor or its affiliates to control the use or ownership of the Property e.g., options to purchase or repurchase the Property; deed restrictions; or restrictive covenants such as those that limit the brand of fuel that can be sold on the Property.

**C.** **Condition of Equipment**. If the loan is to enable the Borrower to acquire the Property associated with the operation of a gas station, Indemnitors warrant that all fuel dispensing equipment located on the Property has been tested by an independent contractor within the preceding twelve months and that all leaking or otherwise defective equipment, systems, containment devices, etc., have been or will be replaced or repaired prior to closing.

**D.** Disclosure of Environmental Information.

1. Full Disclosure by Third Party Indemnitor. Third Party Indemnitor represents and warrants that Third Party Indemnitor has provided Borrower with an accurate and complete copy of each record pertaining to the Property, (regardless of origin or method by which it was produced, recorded or preserved), in Third Party Indemnitor's actual or constructive possession, custody or control that pertain to the Property including those that materially relates to: (1) Contamination; (2) Hazardous Substances at the Adjoining Properties; or (3) compliance with any Environmental Law, Institutional Control or Engineering Control concerning the Property.

2. Full Disclosure by Borrower. Borrower represents and warrants that Borrower provided the Environmental Professional who signed the Report with an accurate and complete copy of each record, (regardless of origin or method by which it was produced, recorded or preserved and including all records provided to Borrower by Third Party Indemnitor), in Borrower's actual or constructive possession, custody or control that materially relates to: (1) Contamination; (2) Hazardous Substances at the Adjoining Properties; (3) compliance with any Environmental Law, Institutional Control or Engineering Control concerning the Property; or (4) any other matter addressed by this Agreement.

**E.** Environmental Investigation of Property.

1. Conducted by Independent Environmental Professional. Lender and Borrower represent and warrant to SBA that an independent Environmental Professional has conducted an Environmental Investigation of the Property and that a complete and accurate copy of the Environmental Investigation Report is attached hereto as Exhibit "B".

   a. Lender's Warranty. Lender represents and warrants to SBA that: (1) the Environmental Professional who prepared the Report is not a representative, employee, Associate or affiliate of, Lender or any Person in which Lender has an ownership interest; and (2) no influence has been exerted over the Environmental Professional with regard to the preparation of the Report or the contents thereof by Lender or by any of Lender's attorneys, agents, employees, Associates or affiliates.

   b. Indemnitors' Warranty. Each Indemnitor independently represents and warrants to SBA that to the best of Indemnitor's knowledge: (1) the Environmental Professional who prepared the Report is not a representative, employee, Associate or affiliate of, Indemnitor or any Person in which Indemnitor has an ownership interest; and (2) no influence has been exerted over the Environmental Professional with regard to the preparation of the Report or the contents thereof by Indemnitor or by any of Indemnitor's attorneys, agents, employees, Associates or affiliates.

2. Report Establishes Environmental Baseline of Property. Lender and each Indemnitor independently represent and warrant to SBA that they have no knowledge of any facts or circumstances that could result in the Report containing incomplete or inaccurate information.

**F.** **Execution and Performance of Agreement.** Each Indemnitor independently represents and warrants to SBA and Lender that:

1. Authority and Financial Capability. Indemnitor is either an individual or a duly organized, validly existing business entity in good standing and duly qualified to do business in each jurisdiction where the conduct of its business requires such qualification; and Indemnitor has and will maintain full power, financial capability and authority to enter into this Agreement, and to perform Indemnitor's obligations hereunder.

2. Validity of Agreement. This Agreement is a legal, valid, and binding obligation of Indemnitor enforceable according to its terms.

3. Authority to Sign. Indemnitor has proper authority to execute this Agreement as evidenced by, and has, if required, provided Lender with a complete and accurate copy of a valid, certified resolution or other evidence confirming such authority.

**IV. COVENANTS**

In addition to their obligations and liabilities under applicable law, Indemnitors covenant and agree as follows:

**A.** Borrower Covenants

1. Notice to Lender. Borrower shall immediately notify Lender upon becoming aware of any of the following: (1) Any Release on the Property that must be reported to any Governmental Entity under applicable Environmental Laws; (2) Any Contamination, or imminent threat of Contamination, or any violation of Environmental Laws in connection with the Property or operations conducted thereon; (3) Any order, notice of violation, fine or penalty or similar action by any Governmental Entity relating to Hazardous Substances or Environmental Laws and the Property or the operations conducted thereon; (4) Any expiration or revocation of any required environmental permit, registration or authorization with regard to the Property or the operations conducted thereon; (5) Any Environmental Claim relating to the Property or the operations conducted thereon; or (6) Any matters relating to Hazardous Substances or Environmental Laws that would give a reasonably prudent lender cause to be concerned that the value of their security interest in the Property may be reduced or threatened or that may impair or threaten to impair Borrower's ability to perform any of Borrower's obligations under this Agreement when such performance is due.

2. Use of Property. Borrower shall not allow Hazardous Substances or the occurrence of any Environmental Activity at the Property except as necessary to operate the type of business specified in the Loan Documents.

3. Compliance with Environmental Laws. Borrower shall not cause, commit, permit or allow non-compliance with any Environmental Law, Institutional Control or Engineering

Control with respect to the Property and shall obtain, keep in effect and comply with all permits, registrations and authorizations required by Environmental Laws with respect to the Property and operations conducted thereon.

4. Environmental Insurance. Borrower shall include Lender as a loss payee on all environmental insurance policies held by Borrower relating to the Property.

5. UST Reimbursement Funds. If the Property securing the Loan is associated with the operation of a gas station, Borrower shall register for all participate in any available federal, state or local petroleum storage tank fund programs that Borrower is eligible to participate in, which permitting full or partial reimbursement of costs incurred for the assessment or Remediation of Contamination, even if such program is voluntary.

**B.** Borrower and Third Party Indemnitor Covenants

1. Record Retention. Until the Mortgage Release Date, Indemnitors shall retain and make available to SBA and SBA Lender upon request an accurate and complete copy of each record (regardless of origin or method by which it was produced, recorded or preserved), in Indemnitor's actual or constructive possession, custody or control that materially relates to: (1) Contamination; (2) Hazardous Substances at the Adjoining Properties; (3) compliance with any Environmental Law, Institutional Control or Engineering Control concerning the Property; or (4) any other matter addressed by this Agreement.

2. Control of Property. Prior to the Mortgage Release Date, Indemnitors shall not record or cause to be recorded any document containing a provision that could enable any Person to control the use or ownership of the Property, such as a purchase option; repurchase option; or restrictive covenant such as one that limits the brand of fuel that can be sold on the Property.

## V. REMEDIATION

**A.** **Corrective, Preventive and Remedial Action.** Indemnitors shall, at their own cost and expense, in a manner that is in compliance with all applicable laws, and at times that will not unreasonably interfere with Borrower's use of the Property, promptly undertake, continuously and diligently pursue and complete any and all Remedial Action that is necessary to: (1) Remediate any Contamination; (2) correct non-compliance with any Environmental Law, Institutional Control or Engineering Control concerning the Property; or (3) respond to any threatened or pending Environmental Claim regarding the Property.

**B.** **Limitation on Third Party Indemnitor's Duty to Remediate.** If Third Party Indemnitor is the seller or prior owner of the Property, Third Party Indemnitor's duty under this section of

the Agreement shall be limited to Remedial Action: (1) necessitated by acts, omissions, events or conditions existing or occurring in connection with the condition, use or occupancy of the Property on or before the date title to the Property is transferred to Borrower under the Purchase and Sale Documents as disclosed in the Environmental Investigation Report; or (2) created or caused by Third Party Indemnitor, (including Third Party Indemnitor's employees, representatives, agents, contractors, or consultants), at any time after the date title to the Property is transferred to Borrower. As set forth in Paragraph VII herein, provided that neither SBA nor Lender has acquired title to the Property, Third Party Indemnitor may also limit its duty to Remediate under this Agreement by paying the entire balance due under the Loan Documents including any applicable pre-payment penalty.

**C.** **Remediation Standards**. Remediation required under this Agreement shall, at a minimum, meet the applicable, relevant, and appropriate requirements and standards in the Environmental Laws ("ARARs") that must be met before the responsible Government Entity will issue a No Further Action letter or the written equivalent thereof.

**D.** **Duration of Responsibility to Remediate.** Indemnitors' responsibility for Remediation under this Agreement shall continue until the earlier of: (1) the Mortgage Release Date; or (2) the responsible Governmental Entity issues a No Further Action Letter or equivalent written assurance that the applicable, relevant and appropriate requirements and standards in the Environmental Laws ARARs have been met. Provided, however, that Indemnitors' responsibility for Remediation shall resume if the responsible Governmental Entity thereafter determines that additional Remedial Action is necessary with respect to any Contamination covered by this Agreement.

## VI. INDEMNIFICATION

**A.** **SBA and Lender's Right to Indemnification.** Except as provided below, upon demand by an Indemnified Party, Indemnitors agree to indemnify and defend (by counsel selected by Indemnitors and reasonably acceptable to SBA and Lender) Indemnified Parties from and against any and all "Environmental Risks." For purposes of this Agreement, "Environmental Risks" means and includes any and all actual or threatened losses, (including loss of use and diminution in value of the Loan or the Property), all direct and indirect costs associated with Remedial Action (including the repair, replacement or restoration of improvements and equipment; and monitoring and other closure requirements imposed by any Governmental Entity), liabilities, demands, claims and causes of action (including those asserted by third parties for personal injury, illness, death, and damage to real and personal property), damages (including natural resource damages, consequential damages and punitive damages), expenses (including experts' and consultants' fees and disbursements), reasonable attorneys' fees and disbursements for in-house and outside counsel (including those incurred

at trial, on appeal, or in enforcing this Agreement, and regardless of the outcome), fines, assessments, penalties, forfeitures, judgments, settlements, orders, equitable relief of any kind, suffered, paid, incurred by, or sought from an Indemnified Party by any Person in connection with, in whole or in part, or arising or allegedly arising, directly or indirectly out of: (1) the inaccuracy or breach of any representation, warranty or covenant contained in this Agreement; (2) the presence, suspected presence, or threat of Contamination; (3) non-compliance with any Environmental Law, Institutional Control or Engineering Control; (4) any Environmental Claim; or (5) the filing or imposition of any environmental lien against the Property.

1. Limitation on Third Party Indemnitor's Duty to Indemnify. If Third Party Indemnitor is the seller or a prior owner of the Property, Third Party Indemnitor's duty to indemnify and defend Indemnified Parties shall be limited to Environmental Risks arising from acts, omissions, events or conditions existing or occurring in connection with the condition, use or occupancy of the Property: (1) on or before the date title to the Property is transferred to Borrower; or (2) created or caused by Third Party Indemnitor, (including Third Party Indemnitor's employees, representatives, agents, contractors, or consultants), at any time after the date title to the Property is transferred to Borrower. As set forth in Paragraph VII herein, provided that neither SBA nor Lender has acquired title to the Property, Third Party Indemnitor may also limit its duty to indemnify under this Agreement by paying the entire balance due under the Loan Documents including any applicable pre-payment penalty.

2. Duration of Indemnitors' Duty to Indemnify. Indemnitors' duty to indemnify and defend Indemnified Parties shall continue until the earlier of the following dates: (1) the Mortgage Release Date or (2) the date after which all pending and potential causes of action that could be asserted against any or all of the Indemnified Parties arising from Contamination or other matters addressed by this Agreement are finally resolved and satisfied in full, dismissed with prejudice and all appeal rights exhausted, or otherwise barred by the applicable statute of limitation.

**B.** Demand for Indemnification or Tender of Defense.

1. Procedure. In connection with any demand for indemnification or defense made pursuant to this Agreement, the Indemnified Party servicing the Loan shall notify the responsible Indemnitor(s) in writing as soon as reasonably practical and shall specify, to the best of Indemnified Parties' knowledge, the facts giving rise to the demand for indemnification or the need for legal defense.

2. Amounts Payable. Any amount to be paid to Indemnified Parties by Indemnitors under this Agreement shall be a demand obligation, immediately due and payable, which Indemnitors hereby promise to pay, and shall bear interest at the monetary default interest

rate provided for in the Note. Payments under this Agreement shall not reduce Borrower's obligations and liabilities under the Note or other Loan Documents.

3. Subrogation. In the event Indemnitors pay Indemnified Parties any amount under this Agreement, Indemnitors shall be subrogated to any rights of Indemnified Parties relating thereto, provided, however, that such subrogation shall not be in derogation of any rights of Indemnified Parties under this Agreement, and shall not be construed to limit the obligations of Indemnitors hereunder.

## VII. THIRD PARTY INDEMNITOR'S ELECTION TO PAY LOAN BALANCE

In the event that either SBA or Lender makes a written demand on Third Party Indemnitor pursuant to this Agreement, and provided that neither SBA nor Lender has acquired title to the Property, Third Party Indemnitor may elect to pay the entire balance due under the Loan Documents, including any applicable pre-payment penalty, in exchange for (1) a release from all liability under this Agreement; and (2) an assignment of SBA and Lender's interest in the Loan Documents to Third Party Indemnitor.

## VIII. RELEASE AND WAIVER

**A.** **Liability Related to Contamination.** Each Indemnitor waives all known and unknown rights and releases all claims and causes of action whether now or hereafter in existence that Indemnitor may have against SBA and Lender related to Contamination at the Property including the right, if any, to indemnification in the event SBA or Lender acquires title to the Property.

**B.** **Alteration of SBA or Lender's Legal Rights.** If any document has been recorded that could alter SBA or Lender's legal rights, remedies or responsibilities such as provisions requiring lien subordination, special notice of default, or forbearance from initiating liquidation activities; or provisions requiring subsequent Property owners to waive legal rights and remedies, release claims or indemnify another Person, Indemnitors waive the right to enforce such provisions against SBA and Lender.

**C.** **Buyout of Duty to Remediate.** If any document gives Third Party Indemnitor the option to pay a lump sum or provide other consideration to Borrower, whether directly or indirectly, in lieu of Remediating the Property, Third Party Indemnitor waives the right to enforce such provision without the prior written consent of SBA and Lender, and Borrower waives the right to receive such consideration without the prior written consent of SBA and Lender.

## IX. SUBORDINATION

**A.** **Priority of Mortgage.** As set forth in greater detail in Exhibit "C", any lien to secure the performance of any of Borrower's monetary or non-monetary obligations to Third Party Indemnitor shall be unconditionally subordinate to the Mortgage.

**B.** **Indemnitor's Consent to Subordination.** Each Indemnitor independently represents and warrants that: (1) Lender has provided Indemnitor with the opportunity to examine the terms of the Mortgage and Loan Documents; and (2) Indemnitor understands that Lender has no obligation to Third Party Indemnitor to advance any funds under its Mortgage or see to the application of the Mortgage funds, and that any application or use of such funds for purposes other than those provided for in the Loan Documents shall not defeat, in whole or in part, the subordination of Third Party Indemnitor's rights and interests in the Property.

## X. LOAN DEFAULT

In the event of default on the Loan, SBA and Lender's obligation to Third Party Indemnitor shall not extend beyond complying with applicable law regardless of conflicting provisions, if any, in the Purchase and Sale Documents such as those requiring notice of Loan default, notice of Mortgage foreclosure, or forbearance prior to initiating liquidation activities on the Loan.

## XI. GENERAL PROVISIONS

**A.** **Consideration.** Indemnitors acknowledge that: (1) they will receive direct and indirect benefits from the Loan; (2) that SBA and Lender have relied and will rely on the representations, warranties, covenants and agreements herein in closing and funding the Loan; and (3) that the execution and delivery of this Agreement is an essential condition but for which SBA and Lender would not make the Loan.

**B.** **Primary and Unconditional Nature of Obligations.** Indemnitors' liability under this Agreement is direct and primary and not that of a guarantor or surety. Unless otherwise specified, the representations, warranties, covenants, agreements and other obligations set forth in this Agreement: (1) are not conditioned on fault or on any other event, occurrence, matter or circumstance; (2) are in addition to, and not in substitution for, any provisions regarding related matters in the Loan Documents; (3) shall not terminate on the Mortgage Release Date or be discharged or satisfied by payment or satisfaction of the Loan or foreclosure of the Mortgage; (4) shall continue in effect after any sale or transfer of the Loan or Property, including transfers pursuant to foreclosure proceedings or in lieu thereof; (5) shall apply regardless of whether or not a Governmental Entity issues an order requiring Remediation, indemnification or any other obligation of Indemnitors under this Agreement; and (6) shall not be affected or impaired by: (a) the voluntary or involuntary liquidation of all or substantially all of any Indemnitor's assets, including liquidation through a receivership, bankruptcy, reorganization or other similar proceedings; (b) SBA or Lender's failure to give any Indemnitor notice of any event or matter under this Agreement, the Loan

Documents, or otherwise; (c) any finding or allegation that Lender or SBA is or was an "owner" or "operator" of the Property; (d) any extension of time for performance under any Loan Document; (e) any exculpatory provision in the Note, Mortgage or other Loan Documents limiting SBA or Lender's recourse to the Property or other security, or limiting SBA or Lender's right to a deficiency judgment; (f) the release of Borrower or any other Person from performance or observance of any agreement, covenant, term or condition in the Note, Mortgage, other Loan Documents or this Agreement; (g) the release or substitution in whole or in part of any collateral for the Loan; (h) the determination by a Governmental Entity that a third party is responsible for the Contamination or its Remediation; or (i) any other act or omission of SBA or Lender other than those specially found by a court of law to have arisen out of gross negligence or willful misconduct.

**C.** **Exhibits Incorporated by Reference.** All Exhibits hereto are deemed a part of this Agreement, incorporated and made a part of this Agreement, including: (1) Exhibit "A" – Legal Description of Real Property Securing Loan; (2) Exhibit "B" – Environmental Investigation Report; and (3) Exhibit "C" – Memorandum of SBA Environmental Indemnification Agreement.

**D.** **Disclaimer**. This Agreement constitutes neither a finding by SBA or Lender, nor knowledge on their part, as to the risks to human health or the environment posed by any Contamination; nor does it constitute a representation by SBA or Lender that the Property is fit for any particular purpose.

**E.** **Headings and Font Style.** The headings and font style (including bold lettering) used in this Agreement are for convenience of reference only and shall not be used to define the meaning of any provision.

**F.** **Rights Not Exclusive.** SBA and Lender's rights and remedies under this Agreement are in addition to any explicit or implied rights and remedies SBA and Lender may have against Indemnitors or any other Person under the Loan Documents, at law, or in equity.

**G.** **No Waiver; Rights Cumulative.** The rights and remedies available to SBA and Lender may be exercised separately or together, and as many times, and in any order that SBA or Lender choose. SBA and Lender may delay or forgo enforcing any of their rights without giving any up. Any waiver, consent or approval under this Agreement must be in writing and signed by all of the parties to be effective.

**H.** **Assignment.** Indemnitors shall not assign, transfer, or delegate this Agreement or any obligation of Indemnitors hereunder without the prior written consent of SBA and Lender which shall not be unreasonably withheld. Any attempted assignment, transfer or delegation without SBA and Lender's prior written consent shall be null and void. SBA and Lender may assign or transfer, in whole or in part, conditionally or otherwise, any interest in this Agreement without impairing the indemnification granted to SBA and Lender, which shall

continue to exist for the benefit of SBA and Lender notwithstanding any such assignment or transfer.

**I.** **Notice.** All notices, demands, consents and other communications required or that any party desires to give under this Agreement shall be in writing and delivered by fax, hand, courier, or by registered or certified United States mail, postage pre-paid, return receipt requested, to the appropriate address or, if applicable, facsimile number, specified at the end of this Agreement or to such other address or facsimile number as Indemnitors, SBA or Lender may designate in a written notice given to all parties to this Agreement. Notices that are delivered by facsimile, hand or courier shall be deemed received upon delivery or transmission. Notices that are deposited in the United States mail shall be deemed received 3 days after the date mailed. Notwithstanding the foregoing, a copy of any notice sent by facsimile shall also be delivered to the addressee by hand, overnight courier or United States mail, and any notice of change of address shall not be effective until actual receipt.

**J.** **Consent to Jurisdiction.** Indemnitors consent to the jurisdiction of the United States District Court for the Federal District in which the Property is located for all purposes in connection with any action or proceeding that arises out of or relates to this Agreement.

**K.** **Construction.** This Agreement shall be governed by and its provisions construed in accordance with Federal law, and to the extent not inconsistent therewith, the laws of the state where the Property is located without regard to its choice of law principles. In the event a court of law or equity finds any provision of this Agreement, or the application thereof to any party or circumstance, to be invalid or unenforceable, the remainder of this Agreement, or the application of such provision to parties or circumstances other than those as to which it is invalid or unenforceable, shall not be affected thereby, and each provision shall be valid and enforced to the fullest extent permitted by law or equity.

**L.** **Modification or Termination.** No amendment, modification, termination, or cancellation of this Agreement shall be effective unless it is in writing signed by an authorized representative of each party.

**M.** **Integration and Entire Agreement.** This Agreement sets forth the entire understanding of the parties and supersedes and merges all other written and oral negotiations, commitments, understandings and agreements relating to the subject matter hereof among the parties including contradictory provisions that would otherwise apply to Indemnified Parties, if any, contained in the Purchase and Sale Documents.

**N.** **Counterparts.** The parties may sign this Agreement in identical counterparts. The signature pages from the separately signed counterparts may be attached to one copy of this Agreement to form a single document.

**O.** **Memorandum of Agreement.** Concurrently with the execution of this Agreement, the parties shall execute a Memorandum of SBA Environmental Indemnification Agreement (the "Memorandum"), in the form attached hereto as Exhibit "C." The executed Memorandum shall be immediately recorded in the official records of the appropriate county or other government office in the state where the Property is located. In the event of a conflict between the terms of the Memorandum and this Agreement, the terms of this Agreement shall control.

**P.** **Intentional Omission or False Statement.** Each party signing this Agreement acknowledges that intentionally falsifying or concealing any material fact with regard to the subject matter of this Agreement may result in prosecution under applicable laws including 18 U.S.C. 1344, which provides for fines up to $1,000,000 and-imprisonment for up to 30 years.

[Add additional signature blocks as necessary including a signature block for the Operating Company, if any, identified in the Loan Documents.]

Borrower:

_____ [Insert name of Borrower]

By: _____

Name and Title: _____

Address: _____

Telephone Number: _____

Facsimile Number: _____

[Add notary acknowledgement]

Third Party Indemnitor:

_____ [Insert name of Third Party Indemnitor]

By: _____

Name and title: _____

Address: _____

Telephone Number: _____

Facsimile Number: _____

[Add notary acknowledgement]

Lender:

_____ [Insert name of CDC or lending institution]

By: _____

Name and Title: _____

Address: _____

Telephone Number: _____

Facsimile Number: _____

[Add notary acknowledgement]

U. S. Small Business Administration

By: _____

Name and Title: _____

Address: _____

Phone Number: _____

Fax Number: _____

[Add notary acknowledgement]

A copy of each notice, demand, and other correspondence with regard to this Agreement must include the SBA Loan Number and be sent to:

Associate General Counsel for Litigation

Office of General Counsel

U.S. Small Business Administration

409 3rd Street S.W.

Washington, DC 20416

And to:

Legal Counsel for _____ [Insert name of SBA District Office]

Name: _____

Address: _____

Phone Number: _____

Fax Number: _____

Exhibit "A"

Legal Description of Real Property Securing Loan
[To be inserted]

Exhibit "B"

Environmental Investigation Report

[To be inserted]

Exhibit "C"

Memorandum of SBA Environmental Indemnification Agreement

**Sample Recording Information**

Return Address:

Please print or type information

Document title(s) (or transactions contained therein): Memorandum of SBA Environmental Indemnification Agreement

Grantor(s):

[Insert names of Borrower(s) and Third Party Indemnitor(s). For individuals, type last name first, then first name and middle initial. Add additional lines as necessary.]

1.
2.
3.

Grantee(s):

1. [Insert name of Lender.]
2. U.S. Small Business Administration, an Agency of the United States Government

Legal Description:

[Insert legal description or abbreviated legal description of Property: i.e., lot, block, plat or section, township, range.]

Assessor's Property Tax Parcel or Account Number at the time of recording:

[Insert Property tax ID number.]

Reference Number(s) of subordinated document(s):

[Insert recording number(s) of Third Party Indemnitor's document(s) to be subordinated to Mortgage securing SBA Loan and other lien instruments.]

Reference Number(s) of Document subordinated to:

[Insert recording number(s) of Mortgage securing SBA Loan and other lien instruments]

**EXHIBIT "C"**

**MEMORANDUM OF SBA ENVIRONMENTAL INDEMNIFICATION AGREEMENT**

SBA Loan No._____

This Memorandum of SBA Environmental Indemnification Agreement ("Memorandum") dated _____ [insert date of SBA Environmental Indemnification Agreement] is executed by _____ (whether one or more, "Borrower"), _____ [insert name of indemnitor(s) not obligated on the SBA Loan] (whether one or more, "Third Party Indemnitor"), _____ [Insert name of Certified Development Company or Lending Institution] ("Lender"), and the U.S. Small Business Administration ("SBA").

## I. PURPOSE OF MEMORANDUM

The purpose of this Memorandum is to provide constructive notice of the un-recorded SBA Environmental Indemnification Agreement of even date with this Memorandum entered into by Borrower, Third Party Indemnitor, SBA and Lender (the "Agreement") pertaining to the real and personal property described therein including the land located at _____ [Insert address] and legally described in Exhibit "A" attached hereto (collectively, the "Property"). The Agreement contains, but is not limited to, the following provisions, which are addressed in greater detail therein:

**A.** Indemnification and Remediation. Borrower and Third Party Indemnitor agree to indemnify SBA and Lender against certain losses, liabilities, damages, etc., including attorney fees and costs, related to environmental contamination associated with the Property and other matters addressed and more fully set forth in the Agreement.

**B.** Indemnitor's Election to Pay Loan Balance. Third Party Indemnitor may, under certain conditions, limit its duty to remediate and indemnify under the Agreement by paying the entire balance due under the Loan Documents including any applicable pre-payment penalty.

**C.** Release and Waiver. Borrower and Third Party Indemnitor release and waive all rights, claims and causes of action against SBA and Lender with regard to environmental contamination at the Property and other matters addressed in the Agreement including the right to enforce any provision recorded in the chain of title to the Property that alters SBA or Lender's legal rights, remedies or responsibilities.

**D.** Warranties and Covenants. Indemnitors warrant, among other things, that there are no documents recorded against the Property that would enable Third Party Indemnitor or its affiliates to control the use or ownership of the Property, such as a right of first refusal, purchase option, repurchase option, restrictive covenant, deed restriction, etc.; and covenant, among other things, not to record or cause to be recorded any such document before Borrower's SBA Loan has been paid in full.

**E.** Subordination. Third Party Indemnitor unconditionally subordinates to SBA and Lender's Mortgage recorded in volume _____ of _____, page _____, under auditor's file number _____, records of _____ County, State of _____ any right, title or interest Third Party Indemnitor has with respect to the Property, whether of record or not, including the following:

Third Party Indemnitor's _____ [Insert description of lien, e.g., deed of trust, mortgage, UCC Financing Statement, etc.] dated _____, recorded in volume _____ of _____, page_____ under auditor's file number _____, records of _____ County, State of _____.

[Add additional blocks as necessary.]

## II. CONFLICTING TERMS OR PROVISIONS

Terms used in this Memorandum that are not defined herein, but are defined in the Agreement, shall have the meaning provided in the Agreement. To the extent any term or provision of this Memorandum conflicts with any term or provision of the Agreement, the terms and provisions of the Agreement shall control.

## III. COUNTERPARTS

The parties may sign this Memorandum in identical counterparts. The signature pages from the separately signed counterparts may be attached to one copy of this Memorandum to form a single document.

[Add additional signature blocks as necessary including a signature block for the Operating Company, if any, identified in the Loan Documents.]

Borrower:

_____ [Insert name of Borrower]

By: _____

Name and Title: _____

Address: _____

Telephone Number: _____

Facsimile Number: _____

[Add notary acknowledgement]

Third Party Indemnitor:

_____ [Insert name of Third Party Indemnitor]

By: _____

Name and title: _____

Address: _____

Telephone Number: _____

Facsimile Number: _____

[Add notary acknowledgement]

Lender:

_____ [Insert name of CDC or lending institution]

By: _____

Name and Title: _____

Address: _____

Telephone Number: _____

Facsimile Number: _____

[Add notary acknowledgement]

U. S. Small Business Administration

By:

_____

Name and Title: _____

Address: _____

Phone Number:_____

Fax Number: _____

[Add notary acknowledgement]

A copy of each notice, demand, and other correspondence with regard to this Agreement must include the SBA Loan Number and be sent to:

Associate General Counsel for Litigation

Office of General Counsel

U.S. Small Business Administration

409 3rd Street S.W.

Washington, DC 20416

And to:

Legal Counsel for _____ [Insert name of SBA District Office]

Name: _____

Address: _____

Phone Number: _____

Fax Number: _____

ATTACHMENTS:

Exhibit "A" - Legal Description of Real Property Securing Loan

# APPENDIX 10: ELECTRONIC SIGNATURES

SBA Lenders may use electronic signatures on SBA forms and other documents requiring signatures provided they comply with the performance standards outlined in this Appendix. Electronic signatures meeting the requirements of this Appendix will be treated as equivalent to handwritten signatures. Nothing in this Appendix affects existing SBA requirements as to who must sign any specific document, or which documents the SBA Lender must retain in the loan file.

SBA's policy is consistent with and requires SBA Lenders to comply with the current version of the National Institute of Standards and Technology (NIST) Digital Identity Guidelines. SBA requires compliance with Identity Assurance Level 2 (IAL2), as described in the NIST Digital Identity Guidelines.

## A. ELECTRONIC FORM OF SIGNATURE:

For the SBA-approved forms of signature, the vendor must comply with "Use of Electronic Signatures in Federal Organization Transactions," Version 1.0, January 25, 2013, section D: "Requirements for Legally Binding Electronic Signatures."

The Electronic Records and Signatures in Global and National Commerce Act (ESIGN) defines electronic signature as "any electronic sound, symbol, or process attached to or logically associated with a contract or record and executed or adopted by a person with the intent to sign the record." Signatories should follow this definition of electronic signature with the exception that SBA will not accept an electronic signature that is solely voice or audio. Electronic signatures include digital signatures.

## B. ELECTRONIC SIGNATURE ELIGIBLE DOCUMENTS:

1. Unless otherwise prohibited by law, SBA Lenders may use electronic signatures on the documents referenced below (collectively referred to as "Eligible Documents"), provided that the signatories comply with the standards outlined in this Notice. Electronic signatures cannot be used on any document identified below if the recording office requires wet ink signatures.
    a. Application Documents: Electronic signatures may be accepted on all documents requiring signatures.
    b. Loan Closing Documents: Electronic signatures may be accepted on all documents requiring signatures.
    c. Secondary Market Sale Documents: Electronic signatures may be accepted on all documents requiring signatures.

d. Servicing Action – Pre-Disbursement Documents: Electronic signatures may be accepted on all documents requiring signatures, including but not limited to change requests and supporting documentation.

e. Servicing Action – Post-Disbursement Documents: Electronic signatures may be accepted on all documents requiring signatures.

f. Liquidation Documents: Electronic signatures may be accepted on all documents requiring signatures.

g. Litigation Documents: Electronic signatures may be accepted on all documents requiring signatures, unless otherwise specified by a court order.

h. Post Default Action Documents: Electronic signatures may be accepted on all documents requiring signatures.

i. Lender On-Boarding Documents: Electronic signatures may be accepted on all documents requiring signatures, including but not limited to lender participation applications and agreements.

j. Delegated Authority Documentation: Electronic Signatures may be accepted on all documents requiring signatures, including but not limited to supplemental guaranty agreements.

k. Targeted and Full SBA Lender Review Documentation: Electronic Signatures may be accepted on all documents requiring signatures.

2. The use of electronic signatures is voluntary; however, SBA Lenders who choose to use electronic signatures must fully comply with the standards outlined in this Appendix and may be held liable for failure to adhere to these standards. Electronic signatures may not be used for transactions that require filing of security or other documents with a jurisdiction that does not have electronic filing capabilities. SBA Lenders must comply with Uniform Commercial Code (UCC) Article 9-105, which outlines the requirements for electronic chattel paper, and article 3 of the UCC, which outlines the electronic equivalent of a paper promissory note, known as a “Transferrable Record”.

## C. VENDOR/TECHNOLOGY SELECTION REQUIREMENTS:

An SBA Lender must ensure that any electronic signature technology vendor it uses:

1. Complies with Section 101 of the ESIGN Act;
2. Has the experience, capabilities, and expected longevity to meet all SBA electronic signature requirements;
3. Includes vendor agreements that contain express provisions that vendors will comply with all applicable SBA requirements pertaining to this Appendix;

4. Includes vendor agreements language that would ensure that vendor representatives will be available to provide testimony to support the United States government in litigation regarding electronic signature data that will be introduced in court;
5. Meets disaster recovery and archiving requirements; and
6. Has adequate quality control processes.

## D. LENDER LIABILITY FOR FAILURE TO ADHERE TO PRESCRIBED STANDARDS:

The Office of Credit Risk Management (OCRM) will review compliance with the ESIGN Act as well as standards outlined in this Appendix as components of its oversight of SBA Lenders.

As with all Loan Program Requirements, SBA Lenders may be held accountable for not complying with the electronic signature standards and requirements set forth in this Appendix.

## E. QUALITY CONTROL:

SBA Lenders must ensure their electronic signature policies and procedures meet all requirements including their own oversight of the electronic signature process.

## F. RECORD RETENTION:

SBA's record retention requirements are the same for both wet ink and electronic signatures (see Appendix 11, Record Retention Requirements). When wet signatures are obtained on original hard copies, the SBA Lender must maintain the hard copy with wet signature in its loan file. For records signed electronically, the audit trail as well as any computer systems (including hardware and software), controls, and documentation must be readily available for, and subject to, SBA inspection for the same periods as records signed in wet ink.

An SBA Lender's system must be able to reproduce electronic records as accurately as if they were paper when printed or viewed. These records must be made available to SBA on request.

## APPENDIX 11: RECORD RETENTION REQUIREMENTS

SBA's record retention requirements are the same for both wet ink and electronic signatures. When wet signatures are obtained on original hard copies, the SBA Lender must maintain the hard copy with wet signatures in its loan file unless otherwise specified below. These record retention requirements supersede all previous record retention guidance in prior SOPs.

A. **7(a) Lenders:**

1. Lenders must retain the original Note; Guaranty(ies); Security/Collateral documents such as mortgages, deeds of trust, security agreements; SBA application (SBA Form 1919 and any other application documents); any SBA Form(s) 159; and any SBA Environmental Indemnification Agreement. Hard-copy records of those documents requiring original signatures must be retained unless the original signature was made electronically in accordance with applicable standards governing electronic signatures. (See Appendix 10, Electronic Signatures, for guidance on electronic signature standards.)
2. Federally-regulated Lenders must comply with the requirements of their FFIR's requirements governing how long to retain documentation.
3. SBA Supervised Lenders must comply with 13 CFR § 120.461.

B. **CDCs:**

1. CDCs may retain scanned copies of documents unless this paragraph specifies that the original document(s) must be retained by the CDC. CDCs must retain the original:
    l. SBA Form 1244, Application for Section 504 Loan;
    m. SBA Form(s) 159; and
    n. Any SBA Environmental Indemnification Agreement.

    Hard-copy records of those documents requiring original signatures must be retained unless the original signature was made in accordance with applicable standards governing electronic signatures. (See Appendix 10 for guidance on electronic signature standards.)
2. Inquiries, partial applications, and applications withdrawn, canceled, or denied by the CDC or SBA must be kept for 2 years after notification of incomplete application, withdrawal, cancelation, or decline. After 2 years, the files may be destroyed.
3. General correspondence must be kept for 1 year. Case-specific correspondence should be filed in the case file.
4. Paid off loan files (including the original application file, servicing file, and closing file), must be kept for 6 years after the loan was paid in full.
5. Files from liquidated loans (including the original application file, closing, and servicing files), must be kept for 6 years after the loan was charged off.

CDC Operational Financial Records must be retained for 6 years unless otherwise indicated by SBA.

# APPENDIX 12: SBA EMAIL ADDRESSES

**For the 7(a) and 504 Loan Programs:**

Birminghamtops@sba.gov Regular SBA Disaster loans

CAFSQuestions@sba.gov the SBA Loan System entry and questions

CLS@sba.gov CAFS/CLS account set up, passwords, changing institutions

Compliance Codes Resolution:
For 7(a): 7aComplianceCheck@sba.gov For 504: 504Questions@sba.gov

COVIDEIDLServicing@sba.gov General questions on COVID EIDL loans (i.e., loan subordination)

DelegatedAuthority@sba.gov All delegated authority inquiries (nominations, renewals, etc.)

EnvironmentalAppeals@sba.gov

Non-Delegated Processing: SBA Lenders who believe that an environmental decision that has been rendered by SBA is inconsistent with the SOP or this Notice may appeal the decision by forwarding a copy of the decision, along with an explanation of how the determination is perceived to be inconsistent with the SOP or this Notice to EnvironmentalAppeals@sba.gov.

Delegated Processing: SBA Lenders cannot seek SBA approval of the Environmental Investigation, but they may continue to contact EnvironmentalAppeals@sba.gov when relying solely upon paragraph d. ix, "Other Factor(s)" for disbursement in the presence of Contamination.

EnvironmentalQuestions@sba.gov: To reach SBA District Counsel, and to ask environmental questions, and for assistance with the Environmental Review process and meeting Loan Program Requirements.

EnvironmentalReviews@sba.gov: For notifying SBA District Counsel that the SBA Lender has uploaded relevant environmental information in the SBA Loan System: Subject line as follows: DISTRICT OFFICE – APPLICATION NUMBER - LOAN NUMBER - LOAN NAME (no spaces in the loan number). Example: "SAN FRANCISCO DISTRICT OFFICE – 98765432 - 1234567810 – ABC CLEANERS". Do not include the environmental reports or attachments.

Franchise@sba.gov: Questions to the SBA Franchise Committee regarding SBA's franchise policy, brand eligibility determination, Franchise Directory, appeals and reconsiderations.

LenderMatch@sba.gov Questions on SBA's Lender Match

OCRM@sba.gov General email account for OCRM inquiries; Email that may be used when the SOP indicates that something should be submitted to D/OCRM

OCRMFraudNotification@sba.gov Notify OCRM of fraud or suspected fraud

OCRMInvoice@sba.gov Risk-Based Review invoices

Sacramento504Register@sba.gov Registration of personnel in order to request Document Verification regarding alien status

SizeStandards@sba.gov Questions on SBA size standards

SNOMemos@sba.gov Submission of Statement of No Objection - The SBA Lender must submit the Applicant's statement of no objection signed by the appropriate ethics official of the pertinent department or military service if its sole proprietor, general partner, managing member, officer, director, or stockholder with a 10% or more interest, or a Household Member of such individual, is an employee of another department or agency of the Federal Government (Executive Branch) in a grade of at least GS-13 (or its equivalent).

**7(a) Loan Program (Only):**

7aDelegatedLoanApps@sba.gov This email account is reserved for 7(a) Lenders with delegated authority to ask questions about a specific loan application or to request an exception to policy. Lender is to provide a summary of the facts and information that identifies the specific application (e.g., owner name, project address) - SBA will not be reviewing the entire case file or multiple attachments.

7aDenials@sba.gov Communication regarding 7(a) guaranty denials or partial denials

7aLoanMod@sba.gov Used for loan modification requests prior to final disbursement

7aLoanProgram@sba.gov General inquiries regarding the status of loans being processed by the Loan Guarantee Processing Center

7aPortfolioTransfers@sba.gov Submission of requests for consent for transfers involving more than one SBA 7(a) loan

7aQuestions@sba.gov For questions about 7(a) Loan Program Requirements and policy

7(a) Upfront Guaranty Fee issues and refunds – Email the appropriate Commercial Loan Servicing Center

DFCActionDesk@sba.gov Loan Transfers: When a transfer involves more than one SBA 7(a) loan, prior to conducting a review for approval, Lenders must pay all outstanding SBA receivables that are more than 30 days in arrears. Lenders must contact this email address in advance of their consent request for information on any SBA receivables outstanding.

FSC.Servicing@sba.gov General inquiries for 7(a) servicing

LSPAgreements@sba.gov Submission of LSP agreements to the LGPC for review

**504 Loan Program (Only):**

504LoanAuth@sba.gov For questions on completing the 504 Loan terms and conditions and using the SBA Loan System to create the Loan terms and conditions.

504Questions@sba.gov For questions about eligibility, loan structure, loan status, processing, servicing, appraisals, pre-application clearance items, environmental reviews, expedited requests. To withdraw a loan after it has been accepted into processing, notify SLPC at this email. Do not mark the loan as withdrawn in the SBA Loan System without notifying SLPC of this change.

504Requests@sba.gov Submission of: Request for permanent CDC status or a single 1-year extension of CDC's probationary status (also cc the Lead District Office); Request for CDC Mergers; Application for Priority CDC Status; CDC name change requests; CDC's Uncompensated Officers or CDC's Board of Directors, or Executive Committees; Changes to Loan Committees; Pre-approval of professional service contracts in accordance with 13 CFR § 120.824 (see Section A, Ch. 5, Para E.6.a., Professional Services Contractors, in this SOP for more information); Changes in CDC Governing Documents; Changes of CDC Contact Information; Litigation or other Legal Proceedings

CDCAnnualReports@sba.gov Submission of: Annual Report (also cc the Lead District Office); Renewal of ALP CDC designation; Renewal request of PCLP CDC designation

OCA1081@sba.gov Electronic submission of Form 1081 in lieu of hard copy

PCLPQuarterlyReport@sba.gov Submit to OCRM the SBA Form 2233, Quarterly PCLP Summary of LLRF Balances; report and reconcile any discrepancies between the Quarterly PCLP List of Required LLRF Deposits and its records. PCLP CDCs also have the option of submitting these reports through the Corporate Governance Repository located on the Capital Access Financial System (CAFS) under the CDC Online function. Use of the Corporate Governance Repository will avoid email size limitation.

SLPC.e504Help@sba.gov Questions regarding the SBA Loan System web screens for 504 loan application

# APPENDIX 14: 7(A) DEBT REFINANCING REQUIREMENTS

This Appendix consolidates the debt refinancing requirements applicable to all 7(a) loan programs. All chapters must comply with the requirements set forth herein. Program-specific requirements are identified in the Program-Specific Requirements section at the end of this Appendix.

## A. GENERAL REQUIREMENTS

13 CFR §§ 120.140(j)(1) and 120.201 SBA-guaranteed loan proceeds may not be used to pay a creditor in a position to sustain a loss (including the same institution's debt). This includes any refinancing that will shift all or part of a potential loss from the original lender to the SBA. The debt to be refinanced must be, and must have been, current for at least the last 12 months or for the life of the loan, whichever is less. "Current" means that a required payment has not remained unpaid for more than 29 days. A loan that has matured and not been paid within 29 days of the maturity date is not current and is not eligible for refinancing.

1. Loan proceeds may be used to refinance the following types of business debt.
    a. Any debt structured with a demand note or balloon payment;
    b. Debt with an interest rate that exceeds the SBA maximum interest rate based on size or term;
    c. Credit Card Debt Used for Business Expenses - The Applicant must certify that the proceeds from the debt were used exclusively for the Applicant's business and were not used for any ineligible purpose as set forth in 13 CFR § 120.130. If a Lender submits a loan with proceeds refinanced from credit card debt where the Applicant certified that the proceeds from the debt were used exclusively for the Applicant's business, but the Applicant certification is determined to be invalid, SBA will not use this as a basis to deny or repair the guaranty purchase request. The Lender can rely on the Applicant certification;
    d. Debt that is over-collateralized based on 7(a) collateral requirements–- see Appendix 19: 7(a) Collateral Requirements, which describes SBA's collateral requirements used to determine if a loan is "fully secured;"
    e. Revolving lines of credit (short-term or long-term) where the original lender is unwilling to renew the line, or the Applicant is restructuring its financing in order to obtain a lower interest rate or longer term;
    f. Debt with a maturity that was not appropriate for the purpose of the financing (e.g., a 3 year term loan to finance a piece of equipment with a useful life of 15 years);
    g. Debt used to finance a change of ownership of a going concern business;

i. See Appendix 15: 7(a) Changes of Ownership for debt refinancing rules related to changes of ownership.

ii. Seller debt structured in conjunction with a 7(a) change of ownership transaction is eligible to be refinanced after it has been in place and current for 36 months.

h. Debt reflected on the Applicant's business balance sheet is eligible for refinancing if the debt is reflected on the Applicant's business tax returns (Schedule C for sole proprietorships) showing the interest expense associated with the debt.

i. Home Equity Line of Credit (HELOC): If the debt is in the form of a HELOC, the Applicant must certify that the amount being refinanced was used exclusively for business. If a Lender submits a loan with proceeds refinanced from debt in the form of a HELOC where the Applicant certified that the proceeds from the debt were used exclusively for the Applicant's business but the Applicant certification is determined to be invalid, SBA will not use this as a basis to deny or repair the guaranty purchase request. The 7(a) Lender may rely on the Applicant certification.

j. A Lender may refinance an existing non-SBA-guaranteed loan or Borrower debt from another lender if the new loan meets the SBA 10 percent improvement to installment payment amount requirement in Paragraph f. below.

2. Factoring agreements are not eligible for refinancing.

3. Sales-Based Repayment Agreements (e.g.; Merchant Cash Advances) are only eligible for refinancing if the original agreement has been converted to a term loan, has amortized for at least 24 months, and no additional Agreements have been implemented since the conversion of the prior agreement(s). If the Sales-Based Repayment Agreement is still active, it is not eligible for refinancing.

4. Refinancing Same Institution Debt (SID). Refinancing of SID may be processed under a Lender's PLP authority. In addition to the requirements in this subparagraph, all conditions of this Appendix must be met.

a. In accordance with 13 CFR § 120.452, a Lender may not use delegated authority to reduce the Lender's credit exposure to the Applicant.

b. An SBA-guaranteed loan may not be used to refinance SID where there is an appearance that the Lender will shift to SBA all or part of a potential loss from that same debt. (13 CFR § 120.201)

c. The Lender must include the following in their loan file:

i. Include a transcript showing the due dates and when payments were received as part of its analysis and recommendation for the prior 36 months, or the life of the loan, whichever is less; and

ii. Explain in writing any late payments and late charges that have occurred during the last 36 months. (Late payments are defined as any payment made beyond 29 days of the due date.)

d. SBA does not consider the following to be refinancing of SID:

i. The debt is an interim loan that has been made for other than real estate construction purposes and was approved by the Lender within 90 days prior to the issuance of a PLP loan number; or

ii. The debt is a construction loan that has not been disbursed at the time the PLP loan number is issued.

iii. When there is an Initial Acquisition change of ownership and the seller's loan is being paid off with proceeds from the Borrower's loan.

e. Refinancing a same institution 7(a) loan: A Lender may refinance its own 7(a) loans via delegated processing only if:

i. It is unable to modify the terms of the existing loan because a secondary market investor will not agree to modified terms, or

ii. An increase in the amount of an existing SBA-guaranteed loan is not possible.

5. Refinancing a 7(a) loan of another Lender. Proceeds may be used to refinance existing 7(a) loans from other Lenders provided the conditions of this Appendix are met. Any applicable subsidy recoupment fees will apply.

6. Refinancing a SBA 504 with a 7(a) loan. Refinancing an existing 504 loan can be processed by non-delegated or delegated authority if:

a. The conditions of this Appendix are met, and either;

i. Both the Third Party Loan and the 504 loan are being refinanced; or

ii. The Third Party Loan has been paid in full and the 504 loan needs to be refinanced as part of a larger transaction to provide funding for expansion of or renovations to the Project Property.

NOTE: Any applicable 504 prepayment penalties will apply. The 7(a) Lender may not solely refinance the TPL's loan for an existing 504 project.

7. Ten Percent Improvement to Installment Payment Amount. When refinancing debt, the new installment payment amount must be at least 10 percent less than the existing installment amount(s) in aggregate. If other debt is being refinanced at the same time, such debt in the aggregate may be included in the installment payment improvement calculation. If the note terms include an escalating payment structure, the new installment amount must be at least 10 percent less than the expected installment amount within the next 12 months. The following exception applies: Debt (short-term or long-term)

structured with a demand note or balloon payment, credit card obligations and HELOC used for business-related purposes, and revolving lines of credit (short-term or long-term) where the original lender is unable or unwilling to renew the line or the Applicant is restructuring its financing in order to obtain a lower interest rate or longer term;

8. When refinancing debt, the loan application must include:
    a. A written analysis that addresses the following issues:
        i. The reason the debt was incurred;
        ii. The factor(s) that support that the proposed refinancing will not pay a creditor in a position to sustain a loss;
        iii. The reason for restructuring the debt (for example, over-obligated or imprudent borrowing);
        iv. How the new loan will improve the financial condition of the Applicant;
        v. An itemization of all debts being repaid by loan proceeds when the individual creditor is to be paid $10,000 or more, and/or the loan number and dollar amount of any existing SBA being debt refinanced
        vi. The reason(s) the Lender believes the debt to be refinanced no longer meets the needs of the Applicant
    b. Supporting documentation for each debt to be refinanced: Lenders are required to:
        i. Retain copies of the note(s) being refinanced, security agreements, leases, and other documentation evidencing the debt to be refinanced. If submitting to LGPC for non-delegated processing, Lenders must include this documentation with the application.
        ii. Include, when applicable, a copy of the most recent credit card statement evidencing the holder of the account and the current balance.
9. The SBA Terms and Conditions must include:
    a. In the Use of Proceeds section, the refinancing must be specifically identified;
    b. An itemization of all debts being repaid by loan proceeds when the individual creditor is to be paid $10,000 or more; and/or
    c. The loan number and dollar amount of any existing SBA being debt refinanced.
10. Other conditions that apply to debt refinancing:
    a. SBA guaranteed loan proceeds may not be used to refinance debt originally incurred for an ineligible SBA purpose at the time it was originally made unless the condition causing the ineligibility no longer exists.
    b. A 7(a) loan may not be used to refinance a debt owed to a Small Business Investment Company (SBIC) or a New Markets Venture Capital Company 13

CFR § 120.130(b).

c. The payment of trade payables is not considered to be debt refinancing.

11. Interim Advances: For loans processed on a delegated or non-delegated basis, after the loan has received an SBA loan number and prior to disbursement, a Lender or an affiliate of the Lender may make interim advances (also known as bridge loans) and 7(a) loan proceeds may be used to reimburse the interim advances. Lender notification to SBA of such advances is not required.

## B. PROGRAM-SPECIFIC REQUIREMENTS

The following exceptions and additional requirements apply for each loan program. Where a program states "All General Requirements apply," lenders must refer to the General Requirements section of this Appendix for the applicable collateral standards.

1. Standard 7(a) Loans
    a. All debt refinancing requirements for Standard 7(a) loans are set forth above.
2. 7(a) Small Loans and Express Loans:
    a. All general debt refinancing requirements apply. A written credit memorandum is not required; however, supporting documentation for the debt being refinanced must be retained.
    b. The requirements outlined in paragraph d. Refinancing Same Institution Debt (SID) above also applies to SBA Express Loans, including that a Lender may not use delegated authority to reduce the Lender's credit exposure to the Applicant (13 CFR § 120.452).
3. 7(a) Manufacturers' Access to Revolving Credit (MARC) loans
    a. All debt refinancing requirements for MARC loans are set forth above with the following exceptions:
        i. The only debt eligible to be refinanced with MARC loan proceeds is debt in which the original purpose of the debt to be refinanced was for working capital purposes.
4. Working Capital CAPLine:
    a. All debt refinancing requirements for Working Capital CAPLines are set forth above with the following exceptions:
        i. Proceeds from a Working Capital CAPLine may only refinance existing short-term revolving debt under the following conditions:
            a) The short-term revolving debt must be terminated after it is paid off with the CAPLine;
            b) Depending on whether the CAPLine will be disbursed based on a

Borrowing Base Certificate (BBC) or not, the Borrower has either a borrowing base or collateral sufficient to support the Working Capital CAPLine plus any other short-term debt that is not being refinanced;

c) If the application includes the refinancing of same-institution short-term revolving debt, and if the Applicant defaults on the SBA-guaranteed Working Capital CAPLine within 90 days of initial disbursement, there will be a presumption that the loan proceeds were used to pay a creditor in a position to sustain a loss causing a shift of all or part of the loss to SBA in violation of 13 CFR § 120.201 and SBA may deny liability on the guaranty;

d) The loan should be secured with at least the same collateral and lien priority as the debt that is being refinanced. However:

i) When the current balance of the debt being refinanced is considered over collateralized relative to SBA collateral requirements and the SBA loan will remain fully secured, the Lender is not required to take the excess collateral.

ii) Substitute collateral may be taken to secure the new loan if it is of comparable value and useful life and is determined to be acceptable by SBA or the Lender under its delegated authority.

5. Contract, Seasonal, Builders CAPLine Loans
    a. Proceeds are not eligible to be used for refinancing existing debt.
6. Export Express Loans
    a. All debt refinancing requirements for Export Express Loans are set forth above.
7. Export Working Capital Program (EWCP) Loans
    a. All general debt refinancing requirements apply to EWCP Loans with the following exceptions:
        i. The loan being refinanced must be terminated after it is paid off with EWCP loan proceeds.
        ii. Lenders may use delegated or non-delegated authority to refinance existing SBA 7(a) guaranteed loans (whether term or line of credit) including existing export-related SBA Express, CAPLine, EWCP, and Export Express and export lines of credit. This includes SBA 7(a) guaranteed same institution loans where there are export sales and only the export collateral may be used to refinance same institution debt . All refinanced debts must be fully supported by active export sales or pending export orders, and the EWCP terms and conditions in the SBA Loan System must specify additional eligible uses of loan proceeds for subsequent draws.

iii. Any business debt refinanced with a EWCP loan must be supported by eligible collateral under a Borrowing Base Certificate or Transaction-Based loan.

iv. The following types of loans are not eligible for delegated processing, and as such must be submitted for non-delegated processing through the Loan Guaranty Processing Center (LGPC):

a) Loans involving a Single Employer 401(k) plan, including Rollovers as Business Start-Ups (ROBS) plan, unless the only investment held by the 401(k) plan at the time of application is the equity in the Applicant business; and

b) Loans involving a Multiple-Employer 401(k) plan (i.e., a plan that holds in trust the assets of other businesses), including a ROBS plan (see SOP 50 10, Section A, Ch. 2, Para. D., 401(k) Plans Including Rollovers as Business Start-Ups (ROBS) Plans, for more information).

v. Prior to the first disbursement, the Lender must ensure:

a) Collateral for the loan being refinanced is transferred to secure the EWCP loan.

b) Any outstanding receivable that would have been applied to pay down the refinanced loan must be applied to pay down the EWCP loan in the same or greater percentage.

vi. Except as stated in the next sentence, if the debt to be refinanced was used in whole or in part to refinance a prior debt, the loan being refinanced, including the associated interest, must be reflected on the Applicant's balance sheet and business tax returns (Schedule C for sole proprietorships) for two full tax cycles prior to application. If the term of the debt to be refinanced is less than the period of two full tax cycles prior to application, the loan being refinanced, including the associated interest, must be reflected on the Applicant's balance sheet and business tax returns for the full tax cycle(s) that occurred between the date of disbursement of the loan being refinanced and the date of application for the EWCP loan.

8. International Trade (IT) Loans:

a. All general debt refinancing requirements apply to International Trade loans. IT loans may include debt refinancing when the refinancing is necessary to improve the competitive position of the business in export markets.

# APPENDIX 15: 7(A) CHANGES OF OWNERSHIP

The following policy and procedures are for all 7(a) loans involving changes of ownership. Change of ownership transactions include credit risks that are not present in other segments of 7(a) lending. Given that change of ownership transactions have grown to be among the largest categories of 7(a) lending, clearer guidelines are provided through this Appendix.

To be eligible for a 7(a) loan to fund a change of ownership, the Lender must demonstrate the Applicant's ability to operate the business and repay the loan from cash flow. Additionally, the Lender must satisfy all financial due diligence requirements set forth in this Appendix.

This appendix is organized as follows: Section A sets forth general change of ownership requirements applicable to all transactions; Section B defines the four transaction categories (Initial Acquisition, Business Expansion, Owner Buyout, and ESOP & Cooperative); Sections C through E set forth uses of proceeds, loan terms, and credit standards.

The use of 7(a) Small loans is not permitted for change of ownership transactions.

Any sections not specifically addressed in this Appendix remain in effect under 7(a) Loan Program Specific rules. If any section of SOP 50 10 conflicts with this Appendix, the rules contained in this Appendix shall govern the change of ownership transaction.

## A. CHANGE OF OWNERSHIP REQUIREMENTS.

(13 CFR § 120.202)

A Borrower(s) (and any individual Co-Borrower as permitted in this Appendix) may use loan proceeds to fund a change of ownership through either a stock purchase (including a stock redemption) or an asset purchase, only under the circumstances described under this Paragraph. An asset purchase will be deemed a change of ownership and must comply with all of the requirements of this Paragraph if the Applicant(s) is purchasing all or substantially all of the assets of the seller's business and is continuing the operations of the seller's business.

The following requirements apply to all change of ownership structures:

1. The change of ownership must promote the sound development and/or preserve the existence of the small business. A 7(a) loan cannot be made solely to an individual. The small business must be either the Borrower or a Co-Borrower.
2. For purposes of the 7(a) loan facilitating the change of ownership, the "Business Purchase Price" excludes all owner-occupied commercial real estate assets being acquired in the transaction. The Lender is required to input the Purchase Price into the SBA Loan System.
    **a.** When real estate is part of the acquisition, the Lender must remove the appraised value of the real estate from the price set by the purchase and sale agreement to determine the Business Purchase Price for purposes of financial due diligence

requirements set forth in this Appendix.

3. Financial due diligence is required on all change of ownership transactions.
    **a.** The financial due diligence requirements are determined by the Business Purchase Price. This threshold for this requirement is independent of total project costs, the application of Borrower equity, structuring of seller debt, or any other measure that would reduce the 7(a) loan amount facilitating the purchase.
    **b.** When a change of ownership transaction requires a Quality of Earnings (QoE) report as part of the necessary financial due diligence, the Lender must use the report's findings to calculate the Debt Service Coverage. If that Debt Service Coverage does not support the business valuation and proposed debt structure, the loan amount must be reduced accordingly. Additional equity (unlimited or limited) may be used to make this adjustment
4. The total debt eligible to support a change of ownership transaction (including seller debt that is not on full standby) is limited to the business valuation amount and must be supported by the Debt Service Coverage of the Applicant.-
5. Lenders must adhere to all requirements pertaining to Business Valuations and Quality of Earnings reports as outlined in Paragraph C.1 of this Appendix.
6. Intangible Assets: A 7(a) loan may be used to finance a change of ownership that includes intangible assets (including, but not limited to, goodwill, client/customer lists, patents, copyrights, trademarks, intellectual property, and agreements not to compete) as long as the financial due diligence requirements set forth in Paragraph C.1 of this Appendix are met.
7. Tax Transcripts: Since the underwriting of change of ownership transactions is managed through the financial due diligence requirements, tax transcripts are considered an extension of the financial due diligence requirements that govern change of ownership transactions. As such, Lenders must comply with the requirements in Section A, Ch. 5, Para. B, IRS Tax Transcript/Verification of Financial Information to validate the information reported by the seller.
8. Seller earnouts/buyer rebates: Seller earnouts are prohibited; however, buyer rebates based on business performance are allowed because this is a benefit to the Borrower.

    If the Borrower receives funds based on a rebate from the seller, proceeds must be applied to pay down the principal balance of the 7(a) loan that funded the change of ownership. In accordance with 13 CFR § 120.223, SBA's requirement to apply seller rebate payments to principal does not trigger a subsidy recoupment fee.
9. Except as provided below, the seller in a **Business Expansion** or **Initial Acquisition** change of ownership transaction may not remain as an officer, director, stockholder, or employee of the business. If a transitional period is needed to assist the business, the

small business may contract with the seller as a consultant for a period not to exceed 24 months (in aggregate, including any extensions).

When the purchaser is buying a business owned by an ESOP, the employees of the business (who are members of the ESOP Trust) may remain as employees of the business after the sale. The seller may stay on as an owner, officer, director, stockholder, or employee of the business or the ESOP when:

a. One or more of the current owners is selling less than their entire percentage of their current ownership (Owner Buyout – Partial Change); or

b. The purchaser is an ESOP or equivalent trust or a cooperative and is acquiring a controlling interest (51% or more) in the employer business (including when the ESOP or equivalent trust or cooperative is acquiring 100% ownership of the small business).

10. The Lender's loan documentation must include:

a. All related business, stock, and asset purchase agreements, including all schedules, and amendments.

b. For transactions involving external capital, the Lender must underwrite and review the terms of all other debt and equity investments. For purposes of change of ownership, any transaction that involved an owner receiving shares in the business in exchange for cash or other contributions would be considered equity investments.

c. A site visit for the Applicant and for the business being acquired. The Lender must document in its loan file the date of the site visit as well as comments. For businesses not operating out of a physical location, the Lender must document what steps were taken to verify the operations of the Seller.

For businesses that operate on a virtual, or otherwise non-customer facing physical location basis (i.e. e-commerce), the Lender may choose not to conduct a physical site visit. The Lender must document in the loan file the basis for determining that a site visit would not materially enhance verification of business operations and may utilize alternative methods, such as virtual meetings or review of business records, to confirm the existence and activity of the business.

d. When real estate is part of the acquisition, a commercial real estate appraisal must meet the requirements in Appendix 19, Para. A.1.d. Real estate appraisal and fixed asset valuation requirements.

e. Please note, for change of ownership transactions which include the acquisition of commercial real estate, the real estate must be structured as either a separate loan or on a blended amortization as outlined in Para. B.1.a.i.

f. With the exception of vehicles as described in Para. C.3.d.i., evidence that all

assets, including transferable licenses (e.g., liquor license) conveyed as a result of purchase are properly secured as collateral by Lender.

1. **Types of Changes of Ownership**

   Change of ownership transactions fall into four categories: Initial Acquisition, Business Expansion, Owner Buyout (Existing and Partial Change), and ESOP and Cooperative.

   Note: **Initial Acquisition** is the default category for 7(a) changes of ownership. For a change of ownership transaction to qualify as a Business Expansion, Owner Buyout, or ESOP & Cooperative, the Lender must document how the Applicant satisfies the requirement in their credit memorandum.

   The Lender is required to input the change of ownership type into the SBA Loan System.

   The following requirements apply to each transaction based on the type of change of ownership being financed:

   a. **Initial Acquisition:** A change of ownership transaction resulting in a new majority or largest individual owner who was not previously employed by, or a direct or indirect owner of, the business being acquired. Initial Acquisitions may be financed under the following circumstances:

      i. A small business that is not an existing owner and is not operating another business in the same NAICS Industry Group (four-digit) is purchasing 100% of the ownership interest in the small business. The acquiring entity will be the Borrower. If, however, the business being acquired will continue to exist as a separate entity, the acquiring entity and the small business being acquired must be Co-Borrowers.

      ii. A Person who is not an existing owner is purchasing 100% of the ownership interest in the small business. The small business and the Person who is acquiring the ownership interest must be Co-Borrowers. In addition, the Note must be executed, jointly and severally, by both the Person who acquires the ownership interest(s) and the small business whose ownership interest is being acquired.

      iii. A small business is acquiring another small business through an asset purchase. The acquiring entity will be the Borrower. If, however, the business being acquired will continue to exist as a separate entity, the acquiring entity and the small business being acquired must be Co-Borrowers.

   b. **Business Expansion:** A change of ownership transaction in which an existing operating business purchases another. Business Expansion transactions may be financed provided the following conditions are met:

      i. An existing small business that has been operating for at least two full fiscal years with the current ownership is purchasing 100% of the ownership

interest in another business.

ii. The acquired business is in the same NAICS Industry Group (four-digit) as the Applicant. A Business Expansion transaction must result in the same or a greater number of full personal guarantors as were in place prior to the transaction. Allowing for additional personal guarantors provides the Applicant with the flexibility to establish a separate ownership structure for the acquired company.

iii. The Applicant operating business is required to be the Borrower. If, however, the business being acquired will continue to exist and operate as a separate entity, the Applicant entity and the small business being acquired must be Co-Borrowers.

**c. Owner Buyout:** A change of ownership transaction that modifies the ownership structure of the Applicant business and does not involve the acquisition of another entity or asset. At least one member of original ownership must remain in place following the transaction and guarantee the loan, regardless of the percentage of ownership post-sale.

For all **Owner Buyout** transactions, individuals not currently employed by the business may only acquire less than 50% of the total equity and may not become the largest direct or indirect shareholder. For purposes of this limitation, indirect ownership interests held through any entity (including holding companies, trusts, or limited partnerships) must be aggregated with any direct ownership interest held by the same individual. Transactions that do not meet this requirement must be processed as **Initial Acquisition.**

Owner Buyouts fall into two categories:

i. Existing Owner Buyout: A change of ownership between existing owners may be financed under the following circumstances:

a) One or more current owners are purchasing the entire interest of another current owner(s), resulting in 100% ownership of the business by the remaining owner(s). The small business and the owner(s) who is acquiring the ownership interest must be Co-Borrowers. In addition, the Note must be executed, jointly and severally, by both the Person(s) who acquire(s) the ownership interest(s) and the small business whose ownership interest is being acquired; or

b) The small business is redeeming the ownership interest of an owner(s), resulting in 100% ownership of the small business by the remaining owner(s). The small business must be the Borrower, and the remaining owner(s) are subject to the requirements for guaranties in Section A, Ch. 5, Para. A, Guaranties.

ii. Partial Change of Owner: Loan proceeds may be used to fund the purchase of all or a portion of one or more owner's interest in the business or of the business itself (e.g., the purchase of treasury stock or membership units) and where at least one of the original owners remains as an owner after the sale and personally guarantees the loan.

a) For Partial changes of ownership: Both the Operating Company and any **new** direct and/or indirect owner (including individuals and entities) who are acquiring any direct and/or indirect ownership interest in the Operating Company must be Co-Borrowers on the new loan, regardless of the percentage of ownership being acquired. Indirect owners must also personally guarantee the loan.

This provision applies only to new owners who did not have equity in the business until the partial change of ownership. For example, a Person who will be a new owner and who is gaining 1% direct and/or indirect ownership in the Operating Company must be a Co-Borrower. As a reminder, because Standard 7(a) processing requirements apply to all change of ownership transactions, in the case of a collateral shortfall (not "fully secured"), SBA requires Lenders to adhere to collateral shortfall rules (see Appendix 19: 7(a) Collateral Requirements paragraph B, subparagraph 1.c.i for all Borrowers and Co-Borrowers.

b) All remaining owners are subject to the requirements for guaranties in Section A, Ch. 5, Para. A, Guaranties.

i) All individuals gaining equity through the transaction, including transactions involving holding companies, are required to be Co-Borrowers. This provision applies only to new owners who did not have ownership in the business prior to this transaction.

ii) Any selling owner (one who receives loan proceeds in exchange for selling part of their ownership) who remains as a direct or indirect owner and owns less than 20% of the business post-sale must provide a full guaranty for the full loan amount pursuant to 13 CFR 120.160(a).

(a) The term of the guaranty must be for at least two years after final loan disbursement.

(b) Lender may use SBA Form 148L or Lender's equivalent. On SBA Form 148L, the term "default" references default as defined in the Note.

(c) SBA does not require these guarantors that are providing a 2-year guaranty to pledge their personal assets (i.e. Personal residences) in the event of a collateral shortfall.

iii) For ESOP transactions, there is a statutory requirement that if the seller of the employer small business remains as a partial owner, the seller must provide a full, unlimited guarantee regardless of ownership – the statutory requirement at 15 U.S.C. § 636(a)(15)(B)(iv)(II) cannot be waived.

c) Multi-step partial changes of ownership are not eligible. A multi-step partial change of ownership occurs when the change of ownership is structured such that some or all of the existing owners are bringing on a new owner(s) via the formation of a new entity that will become the 100% owner of the Operating Company, and where some or all of the existing owners and the new owner(s) will be the owners of the new entity.

d) 7(a) loans may not fund a partial change of ownership in an EPC for a business structured as an EPC/OC due to the regulation at 13 CFR § 120.111. However, 7(a) loans may be used to fund a partial change of ownership in the Operating Company of a business structured as an EPC/OC.

e) The seller may stay on as an owner, officer, director, stockholder, Key Employee, or employee of the business.

**d. ESOP & Cooperatives:** A change of ownership involving Employee Stock Ownership Plans or Cooperatives may be financed under the following circumstances when following their applicable requirements:

i. An Employee Stock Ownership Plan (ESOP) or equivalent trust is purchasing a controlling interest (51% or more) in the employer small business. (Note: any transaction costs associated with the purchase of the controlling interest by the ESOP or equivalent trust, but not the costs associated with setting up the trust, may be included in the use of proceeds.) (13 CFR § 120.352(b)) See Section A, Ch. 2, Para. B., Loans to Employee Stock Ownership Plans (ESOPS), for more information.

a) A small business is obtaining a loan for the sole purpose of re-lending the funds to an ESOP or equivalent trust to acquire a controlling interest (51% or more) in the small business. (Note: any transaction costs associated with making the loan to the ESOP or equivalent trust, but not the costs associated with setting up the trust, may be included in the use of proceeds.) See Section A, Ch. 2, Para. B., Loans to Employee Stock Ownership Plans (ESOPS), for more information.

b) When an SBA loan is used to purchase a business owned by an ESOP for a change of ownership where the ESOP is being dissolved, the employees (owners of the ESOP), except for illegal aliens, may remain

as employees of the business despite other provisions in this SOP to the contrary.

ii. A cooperative is purchasing a controlling interest (51% or more) in the employer small business. (Note: any transaction costs associated with the purchase of the controlling interest, but not costs associated with setting up the cooperative, may be included in the use of proceeds.) These loans may be processed under PLP authority.

**2. Personal Guaranties**

All owners of the Applicant business, and the business being acquired, if it is a Co-Borrower, are subject to the requirements for guaranties in Section A, Ch. 5, Para. A, Guaranties.

For 7(a) change of ownership transactions, except those that involve a selling owner who will retain an indirect or direct ownership interest less than 20%, which must comply with the previously stated guaranty requirements, the percentages for determining who must provide a guaranty will be based on the post-sale percentage of direct and/or indirect ownership in the business.

Additional guaranty requirements specified in this Appendix will apply to all change of ownership transactions.

**3. Uses of Proceeds**

Change of ownership transactions are subject to the following restrictions on Use of Proceeds.

**a. Debt Refinancing**

i. Debt used to finance a change of ownership of a going concern business;

a) To be eligible for refinancing, any seller-financed Note must have been in place and current (not on standby) for at least 36 months following the change of ownership. The refinancing request must meet the SBA's 10 percent improvement to installment payment amount requirement and must not reduce the Lender's exposure.

b) If the change of ownership is between existing owners of a business and existing business debt will be refinanced as part of the transaction, the refinancing must meet the requirements set forth in Appendix 14: 7(a) Debt Refinancing Requirements.

**b. Restrictions on Uses of Proceeds in Change of Ownership Transactions**

13 CFR § 120.130

Loan proceeds may **not** be used for any of the following purposes (including the replacement of funds used or borrowed for any such purpose): Payments,

distributions, or loans to an Associate of the Applicant (as defined in 13 CFR § 120.10), except for compensation for services actually rendered at a fair and reasonable rate or to facilitate 7(a) loans for changes of ownership in accordance with 13 CFR § 120.202 and the guidance in this Appendix in Para.A.1.c.ii. Owner Buyout Partial Change.

i. Change of ownership transactions may include funds for:

a) Working Capital;

b) Borrower out of pocket expenses (including business valuations and QoE); and

c) Owner-Occupied Commercial Real Estate when structured on a blended basis.

**4. Specialty Transaction Structures for Changes of Ownership**

**a. Eligible Passive Companies (EPCs):**

i. An EPC may only use loan proceeds to finance a change of ownership between existing owners of the EPC when the real estate or personal property has been held by the selling owner(s) for at least 36 months.

ii. 7(a) loans may not fund a partial change of ownership in an EPC for a business structured as an EPC/OC due to the regulation at 13 CFR § 120.111. However, 7(a) loans may be used to fund an Owner Buyout – Partial Change of Ownership in the Operating Company of a business structured as an EPC/OC.

## B. LOAN TERMS AND CONDITIONS

1. Loan Maturities

13 CFR § 120.212

7(a) loans are required to have a stated amortization, loan maturity, and may not have a balloon.

a. 7(a) loans that facilitate a change of ownership must not have an amortization that exceeds 10 years.

i. Change of ownership transactions that also include the purchase of real estate (formerly referred to as mixed purpose loans) may be structured as either:

a) Separate loans, one for the change of ownership and one for real estate (including the 504 program) and must comply with the requirements in Para. C.3.c.; or

b) Blended on a weighted average basis, rounded to the nearest full year.

When loan proceeds are used to fund a change of ownership and purchase real estate, the maturity may be blended based on the weighted average use of proceeds. Only the portion of the real estate purchase may have an amortization that exceeds 10-years, up to a maximum of a 25-year term. All other uses of proceeds, including those related to soft costs and working capital, must be allocated a 10-year term. This calculation must be made before the application of any equity and clearly stated in the credit memorandum. The SBA 504 program is not eligible for use on a blended basis.

ii. Lenders may fund a portion of the purchase related to the working assets of the firm onto a line of credit as outlined in Section C. Para. 3.d.i.e of this Appendix.

b. Real estate loans (including acquisition, rehabilitation, renovation, construction, or improvements to leasehold interests in land) must not exceed 25 years, and follow the requirement set forth in both Standard 7(a) and 7(a) Small, as applicable.

## C. CREDIT STANDARDS

### 1. Financial Due Diligence

The financial due diligence conducted on a change of ownership transaction is part of the primary underwriting and eligibility determination.

The out-of-pocket costs associated with all financial due diligence reports may be passed on to the borrower. Any funds expended by the Applicant on the report can count toward the equity injection.

a. Business Valuation Requirements – change of ownership:

i. Determining the value of a business (not including real estate, which is separately valued through a real estate appraisal) is the key component to the analysis of any loan application for a change of ownership. An accurate business valuation is required because the change of ownership will result in new debt unrelated to business operations and the creation of intangible assets. A business valuation assists the buyer in making a determination that the seller's asking price is supported by an independent Qualified Source:

**a) Qualified Source:** (For 7(a) business valuations):

A "Qualified Source" is an individual who regularly receives compensation for business valuations and is accredited by one of the following recognized organizations and is independent of the loan production function, not involved in the approval of the transaction, and must not have the appearance of a conflict of interest:

i) Accredited Senior Appraiser (ASA) accredited through the American Society of Appraisers;

ii) Certified Business Appraiser (CBA) accredited through the Institute of Business Appraisers;

iii) Accredited in Business Valuation (ABV) accredited through the American Institute of Certified Public Accountants; and

iv) Certified Valuation Analyst (CVA) accredited through the National Association of Certified Valuation Analysts.

v) Business Certified Appraiser (BCA) accredited through the International Society of Business Appraisers.

ii. For the individual performing the business valuation to identify the scope of work appropriately, the business valuation must be requested by and prepared for the Lender. The Lender may not use a business valuation prepared for the Applicant or the seller.

iii. The scope of work should identify whether the transaction is an asset purchase or stock purchase and be specific enough for the individual performing the business valuation to know what is included in the sale (including any assumed debt). The business valuation must include the individual's conclusion of value, the qualifications of the individual performing the business valuation, and their signature certifying the information contained in the business valuation.

iv. The business valuation must support the Purchase Price as defined in Paragraph A.1 regardless of how the debt is structured. If the amount paid for the business exceeds the business valuation, the difference must be made up by equity.

a) Lender Verification of Business Valuation Financial Data:

i) Lender must obtain a copy of the financial information relied upon by the individual who performed the business valuation and verify that information against the seller's IRS transcripts to ensure the accuracy of the information.

ii) Quality of Earnings:

(a) For **Business Expansion** and **Initial Acquisition** transactions where the Purchase Price as defined in Paragraph A.1 is equal to or greater than $3 million, the Lender must also obtain a Quality of Earnings (QoE) in addition to the required Business Valuation. The $3 million threshold is determined before the application of buyer equity, seller debt, or other financing sources. Owner Buyout and

ESOP & Cooperative transactions are not subject to the QoE requirement because the existing owner(s) retain operational knowledge of the business and the transaction does not result in a change to the management or operating structure.

(b) QoE: A QoE analysis is a financial due diligence report that examines the reliability, sustainability, and accuracy of a business's historical and projected earnings. The QoE must be performed by an independent, experienced financial professional and must be conducted for the benefit of the Lender. As the QoE is part of the financial due diligence of the transaction, the report may not be prepared by or for the borrower or seller.

(i) The QoE analysis must reconcile the business's accountant-prepared financial statements, tax returns, internal financial statements, and IRS transcript data to produce a normalized, adjusted earnings figure that reflects recurring, arm's-length operations.

(ii) The QoE must include a Cash Proof. For purposes of this requirement, a Cash Proof is a financial analysis that reconstructs cash receipts and disbursements by reconciling bank statement data to the income statement and tax return for each period under review. The Cash Proof is designed to identify discrepancies in income and undisclosed expenses and must be performed on both a trailing 12-month basis and the last two fiscal years.

(iii) The report must identify and document all add-backs and adjustments to the seller's reported earnings, including non-recurring revenue or expenses, above- or below-market owner compensation, related-party transactions, deferred maintenance, and accounting methodology differences between cash-basis and accrual-basis reporting. The QoE must assess the quality and sustainability of the business's revenue base, including customer concentration risk, contract continuity, and the likelihood that existing revenue and margins will be maintained post-sale.

(iv) The Lender must use the earnings from the QoE in the Debt Service Coverage (DSC) determination and retain the QoE report in the credit file.

**2. Underwriting**

**a. Equity Requirements**

i. The minimum equity injection requirement for change of ownership loans is based on the type of transaction.

SBA requires equity injections (Applicant contribution) for change of ownership transactions to be based on the total project cost of the business as defined in Paragraph A.1, plus any additional use of proceeds that are included in the loan request. For **Owner Buyout** transactions, the equity requirement is based upon the purchase price of the business, as reflected in the purchase and sale agreement

Real estate purchased in conjunction with a change of ownership transaction is also subject to the same equity injection requirements. When separated into two loans, the Lender must allocate the equity contribution on a pro-rata basis.

Loans to ESOPs for the purpose of purchasing a controlling interest (at least 51 percent) in the employer small business are not subject to the SBA requirement for equity injection.

a) The following are the minimum equity injection requirements for change of ownership transactions based on their type:

i) Initial Acquisition: 10%.

For Initial Acquisitions, the required equity injection cannot be reduced or eliminated.

ii) Business Expansion, Owner Buyouts, and ESOP & Cooperatives: 10%

(a) For both **Business Expansions** and **Owner Buyouts**, the Lender may reduce or eliminate this requirement if they have determined that the Borrower has sufficient liquidity and working capital to sustain operations following the transaction.

When eliminating the equity requirement, the Lender cannot include permanent working capital in this or any other 7(a) term loan request within 90 days. Any working capital necessary to support the transaction must come from existing cash or a line of credit.

To qualify for the reduction or elimination of the equity injection, the Applicant's balance sheet must not have a negative net worth as of the last fiscal year-end.

(b) Loans for the purpose of purchasing a controlling interest (at least 51 percent) in the employer for purposes of an ESOP are not subject to the SBA requirement for equity injection.

ii. Source of Equity Injections:

a) Unlimited Equity Injection Sources:

i) Cash that is not borrowed, whether on the business's balance sheet or from other sources.

ii) Cash that comes from a personal loan to a guarantor where repayment can be demonstrated to come from a source other than the cash flow of the business (the salary paid to the owner by the business does not qualify).

iii) Grants that do not have any conditional repayment requirements, clawbacks, or any other provision that could require the repayment of the grant during the term of the 7(a) loan.

b) Limited Equity Injection Sources:

The following sources, whether individually or in the aggregate, may provide no more than half of the required Equity Injection.

Additional Limited Equity Sources may be used when additional funds are required to supplement the purchase when the sales price exceeds the value supported by the Business Valuation and Quality of Earnings report. In this situation, any additional funds provided must be on full standby.

i) Standby Debt Agreements:

(a) Debt that is on full standby (no payments of principal or interest for the term of the 7(a) loan) may be considered as equity for SBA's purposes. Lender must use SBA Form 155 or its own equivalent Standby Agreement form, and a copy of the Note must be attached to the standby agreement and included in the credit file.

(b) The standby debt may accrue interest and may be added to the standby debt and amortized after the 7(a) loan is paid in full. Standby Creditor must subordinate any lien rights in collateral securing the loan to Lender's rights in the collateral and take no action against Borrower or any collateral securing the Standby Debt without Lender's consent.

(c) The provider of standby debt may not take an equity investment in the business.

ii) Seller Debt:

(a) Seller debt that is subordinated to the Lender and on full standby (no payments of principal or interest for the term of the 7(a) loan) may be considered as equity for SBA's purposes.

(b) Seller debt structured in conjunction with a 7(a) change of ownership transaction is eligible to be refinanced after it has been in place and current for 36 months.

iii) Non-controlling Minority Equity Investments:

(a) To be considered as eligible equity, the investment may not be subject to any agreement to repay or make distributions to recover the investment prior to release of the SBA guaranty. To qualify as a Non-controlling Minority Equity Investor, the investor must have less than 20% equity in and exert no control over the operating business.

(b) The Lender must review and document the terms of all equity investments, including provisions that are realized upon the sale of the business, in their credit memorandum as part of their underwriting requirements.

(c) When Equity Investments are used to meet the equity injection requirements, distributions to the investor that are not made solely for the purpose of satisfying the investor's tax obligations attributable to the business's income are prohibited until the 7(a) loan has been paid off.

(d) Additional Equity Investments that are not used to meet the equity injection requirements, such as those providing additional liquidity, may receive standard distributions subject to any agreements of the Lender. The Lender may require inclusion of covenants such as DSC into investor agreements, or include DSC covenants into the loan agreement, to ensure that the business has sufficient cash flow to make distributions beyond tax purposes.

**b. Lender's Credit Analysis:**

The Lender's credit memorandum and analysis must address the Applicant's ability and likelihood to repay the loan from the cash flow of the business and past performance by documenting the following:

i. A description of the business, its history, industry, and management structure. The analysis must also include:

a) Description of the Applicant's industry experience and management team, including principal's involvement in the daily onsite management of the business or how the daily operations will be managed if the principals are not there on a daily basis.

b) If the daily operations are handled under a management agreement, Lenders must obtain a copy of the management agreement (unless the

management agreement is part of the franchise disclosure documents for a brand listed on the Franchise Directory), review it to determine if it results in an ineligible passive business, and retain it in their loan file.

ii. Financial analysis of repayment ability:

a) For acquired business, and for Applicants that are an existing operating entity, the Lender's financial analysis must be based on the three most recent year-end historical financial information using the highest level of financial reporting available.

i) Financial reporting is ordered by terms of thoroughness: (1) Audited Financial Statements, (2) Reviewed Financial Statements (including those prepared to AICPA SSARS AR-C 90 standards), (3) CPA Compiled Financial Statements, and (4) Corporate Tax Returns.

ii) For both an operating Applicant and the acquired business, Lenders must also analyze the most current interim financial statement available along with the comparable interim financial statement from the previous year.

b) The Lender must also obtain, review, and verify the Applicant's corporate tax returns against the tax transcripts to comply with the requirements in Section A, Ch. 5, Para. B, IRS Tax Transcript/ Verification of Financial Information.

c) The Debt Service Coverage (DSC) ratio must be satisfied using either the last fiscal year-end or an average of the last two fiscal year-end statements on either a historical or adjusted basis based on the transaction type:

i) Initial Acquisition: 1.25:1

ii) Business Expansion: 1.15:1

iii) Owner Buyout: 1.25:1

iv) ESOP and Cooperative: 1.25:1

d) Historical Debt Service Coverage (DSC):

i) The historical DSC ratio is defined as earnings before interest, taxes, depreciation, and amortization (EBITDA) divided by the combined debt service post-transaction.

ii) Lenders may include an addback for rent payments when the owner-occupied commercial real estate is part of the transaction.

iii) The Lender is required to input the historical DSC into the SBA Loan System.

e) Adjusted Debt Service Coverage (DSC):

When applicable, the Lender is required to input the adjusted DSC into the SBA Loan System.

i) Lender may make prudent adjustments to the cash flow of the acquired entity based on savings that can be realized through the transaction as part of satisfying this requirement. For **Business Expansion** transactions, adjustments may be made based on the combined entities when the acquired business will operate independently following the purchase.

ii) Justification for additions and subtractions to cash flow, such as the following:

(a) Unfunded capital expenditures;

(b) Non-recurring income;

(c) Distributions;

(d) Distributions for S-Corp taxes;

(e) Seller discretionary expenses; and/or

(f) Ownership Compensation.

(i) Adjustments made to ownership compensation must also be substantiated by a global cash flow analysis that demonstrates that the principals have the financial wherewithal to meet their obligations based upon the adjusted compensation proposed and must meet the 1:1 DSC on a global basis.

iii) When using adjustments, the Lender must outline why each adjustment is prudent, necessary, and how it can be supported by the ongoing operations of the business. The justification for each adjustment or add-back must be included in the credit memorandum. The ownership compensation of the Applicant must be sufficient to support their current obligations and living expenses.

iv) Adjustments to cash flow without the Lender's supporting analysis and justification will be ineligible for purposes of determining this core underwriting requirement.

f) The Lender must evaluate the Applicant's post-closing financial projections but may not rely on them to meet the DSC requirement.

g) When a change of ownership transaction includes additional debt to support the purchase that is not on full standby and is structured with interest-only payments, the Lender must apply an amortization that does

not exceed 10-years. This requirement does not apply to lines of credit.

This requirement is to ensure that the business can service all debt associated with the acquisition, regardless of the source or structure.

h) The financial analysis for all Applicants must address the following, as applicable:

i) Global cash flow analysis that includes assessment of impact on cash flow to/from any affiliate business and meets a 1:1 DSC; and

ii) The effect any affiliates may have on the ultimate repayment ability of the Applicant.

iii. Spread of pro-forma Business Balance Sheet (current business balance sheet adjusted for all changes in assets and liabilities as a result of the SBA loan, other debt, any required equity injection, and use of loan proceeds);

iv. Ratio calculations (based on the pro-forma Balance Sheet and historical and projected Income Statements) for the following financial ratio benchmarks: Current Ratio, Debt/Tangible Net Worth, Debt Service Coverage, and any other ratios the Lender considers significant for the business/ industry (e.g., inventory turnover, receivables turnover, and payables turnover, etc.) including discussion of Lender's comparison to industry trends;

v. Analysis of working capital adequacy, at a minimum, over the next 12 months;

vi. Assessment of collateral adequacy adjusted in accordance with Paragraph C.3.c., in this Appendix below to offset risk of default;

vii. Insurance Requirements, including:

a) Life Insurance – on whom and how much. If life insurance is not required, provide justification.

b) Business hazard and liability insurances.

viii. Explanation of and justification for the refinancing of any debts as part of the loan request, along with supporting documentation, in accordance with the debt refinancing requirements in Paragraph A.3.a. above, including a written explanation for any late payments over the past 12 months.

ix. Lender's rationale for recommending approval, including a discussion and analysis of the following:

a) The factors demonstrating the Applicant does not have credit available elsewhere on reasonable commercial terms in accordance with Section A, Ch. 1. Para. H.

b) When 50 percent or more of the loan proceeds will be used for working

capital, Lender must explain in its credit memorandum why this level of working capital is necessary and appropriate for the subject business;

c) Competition;

d) 90+ day delinquencies;

e) Trade disputes;

f) Federal, State, or local citations which would preclude the Applicant from normal business operations;

g) Discussion of any liens, judgments, bankruptcy filings, or pending litigation, including divorce proceedings;

h) If the application involves a franchise (as defined by FTC), the Lender must review any credit information provided, such as the number of failed franchisees and cash flow projections provided by the franchisor; and

i) Discussion of other relevant information

**3. Collateral**

a. To identify collateral, Lenders must use commercially reasonable and prudent practices that are at least as thorough as those used for their similarly-sized non-SBA guaranteed commercial loans. Decisions regarding what collateral must be taken to secure a loan are based on the circumstances of the individual loan, including size, and must meet the minimum requirements in this section.

b. When loan proceeds will be used to refinance existing change of ownership debt, the loan must be secured with at least the same collateral and lien priority as the debt that is being refinanced. When the debt being refinanced is considered to be over-collateralized based on SBA collateral requirements and the SBA loan will remain fully secured, the Lender may approve the release of excess collateral. Substitute collateral may be offered, provided it is of comparable value, useful life, and is determined to be acceptable by SBA or a PLP Lender processing the loan under its PLP authority.

c. Adequacy of Collateral.

i. A Lender may not take any action in connection with an SBA-guaranteed loan that establishes a preference in favor of the Lender (13 CFR § 120.411). The Lender must not have a 7(a) loan in a “piggyback” structure.

a) Piggyback financing occurs when one or more lenders provide more than one loan to a single Borrower at or about the same time, financing the same or similar purpose, and where the SBA-guaranteed loan is secured with a junior lien position or no lien position on the collateral securing the non-guaranteed loan(s). SBA considers “at or about the

same time" to mean loans approved within 90 days of each other.

b) SBA does not consider a scenario where both the SBA-guaranteed loan and the non-SBA guaranteed loan are for working capital, and the non-SBA guaranteed loan is secured only by working/trading assets, to be a piggyback structure.

c) SBA does not consider a shared lien position with the lender (pari passu) to be a piggyback structure when the maturity of the non-SBA guaranteed loan is not shorter than the maturity of the SBA-guaranteed loan.

ii. SBA does not permit its guaranty to be a substitute for available collateral.

iii. When assessing the adequacy of collateral, the Lender must consider the impact that covenants and other restrictions recorded against the collateral may have on its value and marketability. The Lender must document this analysis in the file. Examples of items to review include:

a) Deed restrictions, covenants, easement provisions, reversionary interests, subordinations, leases and options, and other provisions that restrict the use of the property for the benefit of a third party (Note: certain deed restrictions pertaining to the use of the property, which are intended to protect the health and safety of occupants, may be acceptable, e.g., deed restrictions based upon environmental concerns including restrictions on residential use, use as a day care center for children or seniors, use as a school, or use as a hospital); and

b) Engineering Controls that require the Applicant or subsequent owners to install costly devices or structures such as extraction wells or subsurface barrier walls prior to constructing a building, remodeling, or otherwise improving the property.

c) Environmental Indemnification Provisions that run with the land are not eligible and must be removed or waived as to the Federal Government.

d. Collateral Requirements for 7(a) Change of Ownership Loans.

i. SBA considers a loan as "fully secured" if the Lender has taken security interests in all available fixed assets of the Applicant with a combined Net Book Value as adjusted below, up to the loan amount. For 7(a) loans, the term "fixed assets" means real estate, including land and structures, machinery and equipment owned by the business or an EPC.

SBA does not require the Lender to place a lien on vehicles that already have a lien or unless the value of the vehicle (as reported by any of the following: an independent third party (e.g., orderly liquidation value from an appraisal, independent vehicle valuation company or website), or the purchase price

allocable to such a vehicle if the 7(a) loan is being used to purchase the vehicle) is greater than $20,000 at the time the SBA loan number is assigned by SBA. For the purpose of determining whether the Lender must place a lien on a vehicle, Lender must document whether the vehicle already had a lien on it, or the source and dollar amount of the vehicle valuation in the credit memorandum.

a) Used or existing machinery and equipment (excluding furniture & fixtures) may be valued at no more than 50% of Net Book Value or 80% with an Orderly Liquidation Appraisal minus any prior liens for the calculation of "fully secured";

b) Improved real estate can be valued at no more than 85% and unimproved real estate can be valued at 50% of the market value for the calculation of "fully secured" and the value must be determined in accordance with the requirements set forth in Appendix 19 Para. A.1.d. Real estate appraisal and fixed asset valuation requirements.

c) Furniture and Fixtures may be valued at no more than 10% of Net Book Value or appraised value.

d) Lenders must take a security interest in the accounts receivable and inventory of the operating entity. When the Lender takes a security interest in the accounts receivable and inventory, no more than 10% of the current book value of the assets may be used for the fully secured calculation.

e) Working capital lines of credit may be issued alongside change of ownership loans under the following conditions:

   i) As part of the change of ownership transaction, the Borrower has the option to obtain a line of credit (conventional or government guaranteed) to support the working capital needs of the business.

      If the line of credit is required to be in first lien position on the accounts receivable and inventory acquired through the change of ownership transaction (e.g., the trading assets), the Lender must meet the following conditions to release those assets as collateral for the 7(a) change of ownership term loan, and must retain all documentation as evidence of compliance in the loan file (the following is not applicable to lines of credit in second lien position (e.g., SBA Express)):

      (a) Apply no less than 20% and not more than 50% of the day-one line of credit availability to the initial balance on the line of credit. The portion allocated to the line of credit balance must be used to fund the respective portion of the change of ownership transaction.

(i) Day-one line of credit availability is defined as the amount of funds available to the Borrower on the first day that the loan proceeds are available.

*(a)* For an open revolving line of credit, use the committed limit of the loan.

*(b)* For an Asset-based line of credit, use the amount available on the initial borrowing base certificate.

This option allows the Lender the flexibility to fund a portion of the overall purchase price directly onto the line of credit while ensuring that the Borrower has sufficient availability on their line of credit after closing. This flexibility has been structured to ensure that the 7(a) term loan facilitating the change of ownership was reduced by an amount greater than the collateral would otherwise provide for the fully secured determination.

If the day-one line of credit availability would be less than 20% based on the size of the line or collateral advance rates, the Lender is prohibited from using this option.

ii. Collateral shortfall: If there is a collateral shortfall (not "fully secured") on the SBA-guaranteed loan the Lender:

a) Must take available equity in the personal real estate (residential and investment property including other commercial real estate regardless of whether the owner is actively running a business at the investment property) that is solely owned by any Co-Borrowers, direct and/or indirect owners of 20% or more of the Applicant and guarantors except Supplemental Guarantors. For purposes of this requirement, "solely owned" real estate includes property held in an entity that is solely owned, directly or indirectly, by such persons. Liens on personal real estate may be limited to the amount of the collateral shortfall. In addition, liens on personal real estate may be limited to 150% of the equity in the collateral.

b) SBA does not require a Lender to collateralize a loan with real estate (including commercial, residential and investment properties owned by the Applicant or personally by the owners) to meet the "fully secured" definition when the equity in the real estate is less than 25% of the property's fair market value. For this purpose, "lack of equity" means that the property's fair market value, after giving effect to existing liens, does not provide at least 25% equity; the mere presence of a prior lien that restricts or prohibits the placement of a junior lien does not, by itself, constitute "lack of equity" under SBA rules. The Lender must

document in their loan file the source (other than the personal financial statement) used to make the equity determination.

iii. Assets owned by an owner of the Applicant and Spouse:

a) When an individual alone or together with his or her spouse or minor children owns 20% or more of the Applicant, the Lender must consider taking as collateral a lien on personal real estate (including commercial and investment properties not occupied by the Applicant) that is owned individually by the Applicant owner or jointly owned by the individual and his or her spouse or minor children.

b) Real estate transferred by the owner of the Applicant to the non-owning spouse or minor children within 6 months of the date of the application will not be exempt from consideration as available collateral.

## D. SUBMISSION OF APPLICATION FOR GUARANTY

### 1. Contents of Lender's Application for Guaranty & Submission to SBA

For all change of ownership transactions using a 7(a) loan, all information contained in this Appendix must be included with the package.

a. If the loan application is submitted to the LGPC, the business valuation must be submitted as part of the loan application.

b. If the application is submitted under PLP authority, the business valuation and QoE may be obtained and reviewed after the issuance of an SBA Loan Number and prior to closing, so long as they are in process.

c. If the Lender is processing the application under PLP authority, the business valuation and applicable QoE must have been formally engaged (i.e., a vendor must have been retained, and an engagement letter must be in place) at the time that the SBA Loan Number is issued. In situations where financial due diligence is not yet complete, the credit memorandum must include an estimate of the value of the business. Following completion of the financial due diligence requirements, the credit memorandum must be updated, with discussion to include:

d. Updated analysis to include the findings in the QoE, with any impact to DSC ratio calculations; and

e. Business valuation results with any impact to the Purchase Price or equity structure.

# APPENDIX 16: 7(A) MAXIMUM GUARANTY AMOUNTS AND PERCENTAGES

This Appendix consolidates maximum guaranty amount and percentage requirements applicable to all 7(a) loan programs. Program-specific maximums are listed in the Program-Specific Requirements section.

## A. GENERAL REQUIREMENTS

1. Maximum Guaranty Amounts and Percentages

   The maximum dollar amount outstanding of SBA's guaranty to any one business and its affiliates must not exceed $3,750,000 (13 CFR § 120.151). SBA considers an EPC and an OC to be "one business" for this purpose. When calculating the maximum guaranty percentage available to a Borrower and its affiliates, the Lender must include the approved loan amount and any existing 7(a) or 504 loans, including revolving lines of credit. The SBA's guaranty is also known as the "SBA share" or "guaranteed portion."

   a. The maximum guaranty amount is $3,750,000.

   b. The maximum guaranty percentage is:

      i. 85% for loans of $150,000 or less

      ii. 75% for loans over $150,000

   c. Combination of 7(a) and 504 loans.

      i. When an Applicant applies for any combination of 7(a) and 504 loans, the order in which the loans are approved determines the maximum loan and guaranty amount available. Due to statutory requirements, the 7(a) loan should be processed and approved first.

      ii. Lenders must advise the SBA processing centers that there is a companion 504 application to ensure the 7(a) loan is processed and approved prior to the 504 loan application being processed and approved.

   d. Maximum Guaranty Percentage for Multiple 7(a) Loans (13 CFR § 120.210).

      For multiple 7(a) loans approved within 90 days of each other, the gross dollar amounts of the loans are combined. If the combined gross amount exceeds $150,000, then the percentage of guaranty on the combined loans must not be more than 75 percent (subject to the $3,750,000 limit).

      For example, if a business receives an 85 percent guaranty on a loan of $140,000 and submits a second application for $50,000 within 90 days of the first loan's approval, the percentage of guaranty on the second loan must be reduced to 47 percent so the combined guaranty is no more than $142,500, or 75 percent of the total amount of both loans ($190,000).

e. Zero Percent Guaranty Cannot be Provided for Ineligible Purposes:

A 7(a) loan cannot include proceeds for an ineligible purpose or have any portion of the loan made to an ineligible business and no part of an SBA 7(a) loan may be guaranteed at zero percent.

## B. PROGRAM-SPECIFIC REQUIREMENTS

The following exceptions and additional requirements apply for each loan program. Where a program states "All General Requirements apply," lenders must refer to the General Requirements section of this Appendix for the applicable collateral standards.

The following program-specific maximums and rules apply:

1. Standard 7(a) Loans
    a. All general requirements set forth in the General Requirements section above apply. No additional program-specific exceptions.
2. 7(a) Small Loans and SBA Express
    a. The guaranteed amount of all 7(a) Small and SBA Express loans counts toward the $3,750,000 maximum SBA exposure that may be outstanding for all SBA loans to a Borrower and its affiliates at any one time.
    b. The maximum guaranty percentage is:
        i. For 7(a) Small loans:
            a) 85% for loans of $150,000 or less
            b) 75% for loans over $150,000
        ii. For SBA Express loans: 50%.
3. 7(a) Manufacturers' Access to Revolving Capital (MARC) Loans
    a. All general requirements contained in this Appendix apply; subject to maximum loan amount requirements per industry:
        i. Manufacturers (NAICS 31-33): loans less than or equal to $5,000,000, the maximum guaranty amount is $3,750,000.
        ii. All other eligible industries: loans less than or equal to $2,000,000, the maximum guaranty amount is $1,500,000.
    b. The maximum guaranty percentage is:
        i. 85% for loans of $150,000 or less.
        ii. 75% for loans over $150,000.
4. CAPLines (All Variants)

    All general guaranty requirements contained in this Appendix apply to all CAPLines.

5. Export Express Loans
    a. Multiple Export Express loans are allowed up to the program maximum loan amount ($500,000 gross for Export Express). The guaranteed amount of all Export Express loans counts toward the $3,750,000 maximum SBA exposure that may be outstanding for all SBA loans to a Borrower and its affiliates at any one time.
    b. If multiple Export Express loans are approved within 90 days of each other, and the combined gross loan amount of all the Export Express loans approved in that time frame to any one Borrower (including affiliates) exceeds $350,000, then the maximum guaranty percentage on the second loan must be reduced accordingly so the combined guaranty is no more than 75% (subject to the $3,750,000 guaranty amount limit).
    c. The maximum guaranty percentage is:
        i. 90% for loans of $350,000 or less; and
        ii. 75% for loans over $350,000 up to $500,000.
6. Export Working Capital Program (EWCP) and International Trade (IT) Loans
    a. The maximum guaranty amount is $4,500,000.
    b. The guaranty percentage is 90 percent.
    c. Combination of 7(a) and 504 loans.
        i. When an Applicant applies for any combination of 7(a) and 504 loans, the order in which the loans are approved determines the maximum loan and guaranty amount available. Because the 7(a) loan has a lower maximum guaranteed amount, the 7(a) loan should be processed and approved first.
        ii. Lenders must advise the SBA processing centers that there is a companion 504 application to ensure the 7(a) loan is processed and approved prior to the 504 loan application being processed and approved.

# APPENDIX 17: 7(A) LOAN MATURITY REQUIREMENTS

This Appendix consolidates loan maturity requirements applicable to all 7(a) loan programs. Program-specific maturity terms are listed in the Program Specific Requirements section.

## A. GENERAL REQUIREMENTS

13 CFR § 120.212

7(a) loans must have a stated maturity. The loan term must be the shortest appropriate term based on the use of proceeds and the Borrower's ability to repay. A loan's term must be:

1. Working capital or inventory loans and the financing of intangible assets (including goodwill) must not exceed 10 years.
2. Generally, equipment, fixtures, or furniture loans should not exceed 10 years. However, the term may be up to 15 years if the IRS asset class useful life supports the term. The term for a loan to finance equipment and/or leasehold improvements may include an additional reasonable period, not to exceed 12 months, when necessary to complete the installation of the equipment and/or complete the leasehold improvements.
3. Real estate loans (including acquisition, rehabilitation, renovation, construction, or improvements to leasehold interests in land) must not exceed 25 years, unless a portion of the loan is used for construction or renovation of the real estate. If the use of proceeds on a real estate loan includes construction or renovation, an additional period reasonably necessary for the construction or renovation period may be added to the 25-year maximum maturity.
4. Loans for leasehold improvements (except for leasehold interests in land) may not exceed 10 years, plus an additional period reasonably necessary to complete the leasehold improvements, as determined based on the specific nature of the leasehold improvements, but in no case more than 12 months.
5. Mixed purpose loans and loans for all types of changes of ownership: See Appendix 15: 7(a) Changes of Ownership.
6. For loans to farm enterprises:
    a. Where land and structures (including poultry houses) for farming comprise 51% or more of the use of proceeds, the maximum maturity is 20 years.
    b. Where machinery and equipment comprise 51% or more of the proceeds, the maximum maturity is the useful life of the machinery and equipment, not to exceed 15 years, plus an additional period reasonably necessary for installation, which may not exceed 12 months.

## B. PROGRAM-SPECIFIC REQUIREMENTS

The following exceptions and additional requirements apply for each loan program. Where a program states "All General Requirements apply," lenders must refer to the General Requirements section of this Appendix for the applicable collateral standards.

The following program-specific maturity terms and rules apply:

1. Standard 7(a) Loans
    a. All general requirements set forth in the General Requirements section above apply. No additional program-specific exceptions.
2. 7(a) Small Loans
    a. All general requirements set forth in the General Requirements section above apply. No additional program-specific exceptions.
3. SBA Express lines of credit:
    a. SBA Express lines of credit:
        i. May not exceed 10 years inclusive of a term-out period.
        ii. Revolving loans:
            a) Revolving loans of more than 12 months must be structured with a term-out period that is not less than the draw period. Once the loan is amortized, no additional draws are permitted. Under no circumstances may there be any advances after the initial 60 month period.

            For example, the loan can have an 8 year maturity with a 2 year draw period and a term-out period of 6 years. Conversely, a loan with an 8 year maturity cannot have a draw period of 6 years and term-out period of 2 years.

            b) Lenders have the ability to reissue a new SBA Express loan to restructure a current SBA Express loan at any point before amortizing payments begin.

            Option #1 - Line Retention: When reissuing a new SBA Express loan to retain the revolving period, the Lender must address the overall line utilization in their credit memo and justify why the line needs to be retained.

            Option #2 - Extended Amortization: Lenders may reissue a new SBA Express to term out their existing SBA Express loan with a term that does not exceed 10 years. This option expressly allows a Lender to establish a longer amortization term that exceeds an initial repayment

term of the initial SBA Express loan. When utilizing this option, the new Express loan may not have a revolving period.

c) May be established as renewable each year, provided they do not exceed the maximum maturity. Lender may not charge a renewal fee. If the original maturity was for 12 months or less, and the new maturity exceeds 12 months, an additional guaranty fee will be due. See Section A, Ch. 4, Para. C.1.a.v., Additional Guaranty Fee for Extensions of Short-Term Loans.

d) Revolving loans with maturities of 12 months or less may be initially structured without a term-out; however, if the loan is renewed or the maturity extended beyond 12 months, the requirements in Paragraph a)ii) above will apply.

4. 7(a) Manufacturers' Access to Revolving Credit (MARC) Loans

   a. Revolving loans:

      i. Revolving loans have a maximum maturity of 20 years.

         Since revolving MARC loans have a maximum amortization of 10 years, they are not subject to the subsidy recoupment fee.

      ii. Revolving loans of more than 12 months must be structured with a term-out period that is at least as long as the draw period, with no draws permitted during the term-out period.

      iii. Revolving loans may not revolve for more than 10 years. At the end of the revolving period, the loan must be converted to a fully amortizing loan with a maximum additional repayment term of up to 10 years.

      iv. Revolving loans may be established as renewable each year, provided they do not exceed the maximum revolving period of 10 years. If the original maturity was for 12 months or less, and the new maturity exceeds 12 months, an additional guaranty fee will be due.

      v. Revolving loans with maturities of 12 months or less may be initially structured without a term-out; however, if the loan is renewed or the maturity extended beyond 12 months, the requirements above will apply.

5. CAPLines (All Variants)

   a. Working Capital, Contract, and Seasonal CAPLines

      The maximum maturity on a Working Capital, Contract, or Seasonal CAPLine is 10 years. Any CAPLine with a maturity of less than 10 years can be renewed as long as the total revolving repayment period does not exceed 120 months. The renewal is an extension of maturity (not a new loan). Thus, the loan number remains the same. If the original maturity was for 12 months or less, and the new

maturity exceeds 12 months, an additional guaranty fee will be due. See Section A, Ch. 5, Para. C.1.a.v., Additional Guaranty Fee for Extensions of Short-Term Loans.

b. Builders CAPLines

13 CFR § 120.396 The loan must not exceed 60 months plus the estimated time to complete construction or rehabilitation.

c. All CAPLines must have an exit strategy. Final disbursement should occur far enough in advance of maturity so that a sufficient amount of time is available for the assets acquired with proceeds to be converted back to cash and final payment.

d. Contract, Seasonal, and Builders CAPLines that finance a single transaction should have a maturity tied to the seasonal cycle, contract completion date, or project completion date.

e. Loan maturity must not exceed the period of the guaranty.

6. Export Express Loans

a. Export Express loans must have a stated maturity. The loan term must be the shortest appropriate term based on the use of proceeds and the Borrower's ability to repay.

i. Lines of credit must not exceed 7 years.

a) Transactional lines of credit: No disbursement can be made for an export transaction where payment by the foreign buyer will occur after the maturity date of the loan.

b) Revolving loans:

i) Maximum maturity includes any “term-out” period;

ii) May be established as renewable each year provided they do not exceed the maximum maturity.

iii) Lender may not charge a renewal fee. If the original maturity was for 12 months or less, and the new maturity exceeds 12 months, an additional guaranty fee will be due.

b. Export Express Term Loans: All general requirements set forth in the General Requirements section above apply. No additional program-specific exceptions.

7. Export Working Capital Program (EWCP) Loans

a. The EWCP loan term represents the period for which the 7(a) loan commitment has been issued. The Lender may set independent loan maturities (typically on an annual basis) to take place during the loan term.

b. General: The maximum maturity of an EWCP loan is 36 months. The maturity

date is set in terms of the number of months from the date of the Note. SBA's guaranty remains in effect for disbursements made through the maturity date. With the exception of a disbursement made to fund a draw against a Standby Letter(s) of Credit that was issued under the EWCP before the maturity date, disbursements made after the maturity date are not covered under the guaranty. The maturity of the loan is:

i. The date specified in the SBA Loan System. Such date will not be longer than 36 months from the Note date. If the loan is not reissued, or extended, all outstanding amounts are due and payable on that day.

ii. Standby Letters of Credit. Unless SBA provides prior written consent, Standby Letters of Credit supported by an EWCP loan must expire before the loan maturity date. If the Lender receives SBA's prior written consent and makes a disbursement after the maturity date because there has been a draw on a standby letter of credit which was issued under the EWCP prior to the maturity date, such disbursement will be covered by the guaranty.

a) Loan maturity must not exceed the period of the guaranty.

iii. Specific Types of EWCP loans:

a) Transaction-Based Loan: A line of credit that can support a single or multiple transactions during the term of the loan. A Transaction-Based EWCP may be established on a revolving or non-revolving basis based on the needs of the business.

b) Asset-Based Loans (ABLs): ABLs are revolving lines of credit supported by a monthly Borrowing Base Certificate (BBC) that reports levels of assets, typically accounts receivable and inventory, supporting the loan amount. ABLs are typically committed for 12 months and then renewed or re-issued annually.

b. Annual and Renewal Credit Review Requirements for Transaction-Based and Asset-Based (ABLs) EWCP loans

i. On no less than an annual basis, and as part of any renewal of the loan, the Lender must obtain updated year end and interim financial statements and perform a full review of the credit and collateral securing the EWCP loan. The Lender's analysis must document that the Applicant:

ii. Is creditworthy.

iii. Has the reasonable assurance of repayment in a timely manner from the conversion of sales into cash; and

iv. Is in compliance with EWCP program requirements.

v. If the Lender's analysis does not document that all three of the above

requirements are met, no further disbursements may be made, and the loan may not be renewed until the Applicant is able to demonstrate that it meets the above three requirements.

8. International Trade (IT) Loans

    a. All general requirements set forth in the General Requirements section above apply. No additional program specific exceptions.

# APPENDIX 18: 7(A) INTEREST RATE REQUIREMENTS

This Appendix consolidates the interest rate requirements applicable to all 7(a) loan programs. All chapters must comply with the requirements set forth herein unless a program-specific exception is identified in the Program-Specific Interest Rate Requirements section at the end of this Appendix.

## A. GENERAL POLICY ON INTEREST RATES

1. General Policy on Interest Rates 13 CFR §§ 120.213 & 120.214

    a. A loan may have a fixed or variable interest rate. The maximum interest rate that may be established for any 7(a) loan is governed by SBA's regulations on interest rates, which preempts any provisions of a state's constitution or law. The Lender negotiates the interest rate with the Applicant, subject to SBA's maximum allowable rates.

    b. SBA will periodically publish the maximum allowable fixed interest rate in the Federal Register. The maximum allowable fixed interest rate will be the Prime rate in effect on the first business day of the month, plus an allowable spread over Prime, as set forth in the most recent Federal Register Notice. For a listing of the current maximum allowable fixed interest rates, go to SBA's Fiscal Transfer Agent (FTA) Wiki. The maximum allowable fixed rate may only be used by a Lender if such rate will be in effect for the entire term of the loan, without adjustment or reset. Otherwise, the maximum rates for variable rate loans will apply.

    c. For variable interest rate loans, the base rate in effect on the first business day of the month will determine the basis for the initial interest rate for any complete loan application received by SBA during that month. (Note: The date the "complete loan application is received by SBA" is the date the loan is approved and assigned an SBA loan number). The initial note rate must not exceed SBA's maximum interest rate. The basis for the SBA maximum interest rate is an acceptable base rate plus allowable spread. The spread above the base rate as identified in the Note may not be changed during the life of the loan without the written agreement of the Borrower.

    d. Default interest rates are not permitted.

    e. For loans with a variable interest rate, the following terms must be defined in the SBA Loan System and the Note:

        i. Base Rate or Alternative Base Rate

        ii. Spread

            a) There are two acceptable Base Rates:

i) The Prime Rate; or

ii) The SBA Optional Peg Rate.

b) There are three acceptable Alternative Base Rate options:

i) Secured Overnight Funding Rate (SOFR); or

ii) 5-year Treasury Note Rate; or

iii) 10-year Treasury Note Rate.

c) The Prime Rate will be that rate which is in effect on the first business day of the month, as identified in a national financial newspaper or website. This rate may be found in the newspaper on the second business day of the month. If a website is used, please ensure whether it is publishing the current day's rate or the previous day's rate as some newspaper websites publish the previous day's rate. The Optional Peg Rate is a weighted average of rates the Federal government pays for loans with maturities similar to the average 7(a) loan. SBA calculates and publishes the Optional Peg Rate quarterly in the Federal Register. Base Rates will be rounded to two decimal places with .004 being rounded down to .00 and .005 being rounded up to .01.

d) The Secured Overnight Funding Rate (SOFR) will be the daily rate which is reported for the first business day of the month, as identified by the Federal Reserve Bank of New York. SBA recognizes that financial institutions use a range of SOFR products to deliver an equivalent reference rate (e.g., 30-day term SOFR and 30-Day Average SOFR). Lenders may continue to use their established in-house SOFR reference rates of 30 days or less, as these rates closely correlate with the daily SOFR rate.

e) The Treasury Rates included as Alternative Base Rates will be based on the Federal Reserve Select Interest Rates, Treasury constant maturities, publication reported for the final business day of the prior month.

iii. Frequency of change;

iv. Range of fluctuation; and

v. Ceiling and floor (if any).

2. Base Rate, Alternative Base Rate, Allowable Spread, and Frequency (13 CFR § 120.214):

a. A loan may have a variable interest rate. The base rate may be one of the following:

i. The Prime Rate; or

ii. The SBA Optional Peg rate.

b. A loan with a variable interest rate may utilize an Alternative Base Rate. The Alternative Base Rate may be one of the following:

   i. Secured Overnight Funding Rate (SOFR); or

   ii. 5-year Treasury Note Rate; or

   iii. 10-year Treasury Note Rate.

c. The allowable spread when using the base rate (i.e., prime rate or SBA Optional Peg) is determined by the loan amount.

   i. Loans of $50,000 and less: Base rate + 6.5%;

   ii. Loans of $50,001 up to and including $250,000: Base rate + 6%;

   iii. Loans of $250,001 up to and including $350,000: Base rate + 4.5%;

   iv. Loans of $350,001 and higher: Base rate + 3%.

d. When using an Alternative Base Rate, the maximum interest rate (Alternative Base Rate plus spread) is determined by the loan amount with a cap based on the Prime interest rate.

   i. Loans of $50,000 and less: Prime + 6.5%;

   ii. Loans of $50,001 up to and including $250,000: Prime + 6.0%;

   iii. Loans of $250,001 up to and including $350,000: Prime + 4.5%;

   iv. Loans of $350,001 and higher: Prime + 3.0%.

e. The Lender must designate in its application for guaranty the amount of the percentage spread to be added at each adjustment date. The same spread must be used for all adjustments.

3. Policy on Variable Interest Rates

   a. Standard Policy:

      SBA's maximum allowable interest rate applies both to the initial Note rate on a variable rate loan and to the combined rate that is obtained by adding the spread to either the base rate or Alternative Base Rate as outlined in Appendix 18: 7(a) Interest Rate Requirements. The spread applied to adjustments must be less than or equal to the maximum allowed by SBA at the time of origination.

   b. Post-Approval Changes to the Interest Rate:

      i. Pre-Disbursement Changes: After loan approval and prior to first disbursement, the Lender may change the initial Note rate, including changing the base rate, Alternative Base Rate, the spread over the base rate or Alternative Base Rate, or change from a fixed rate to a variable rate, or from a variable rate to a fixed rate, provided the new interest rate does not exceed

the maximum allowable interest rate at the time of the loan application. The Lender must obtain the Borrower's written consent to the change in the interest rate (separate and apart from executing the loan documents) and must either notify the LGPC of the change or make the change through E-Tran Servicing, or successor SBA Loan System.

For example, an SBA-guaranteed loan was approved with a variable rate. Since the loan was approved, the Prime rate changed. The Borrower has asked the Lender if the loan can be switched to a fixed rate. If the loan has not been disbursed and the fixed rate selected does not exceed the maximum allowable fixed rate at the time of loan application, the Lender may make this change per the Borrower's request.

ii. Post-Disbursement Changes: After the loan is disbursed, on a variable rate loan, the Lender may change the base rate, Alternative Base Rate, or spread as long as the change is based on a method permitted when the loan was approved and is consistent with the interest rate regulations at the time the loan was approved. The Lender must obtain the Borrower's written agreement and must either notify the CLSC of the change or make the change through E-Tran Servicing, or successor SBA Loan System. For further guidance, see SOP 50 57.

c. Frequency of Interest Rate Adjustment:

i. The first adjustment may occur on the first calendar day of the month following initial disbursement, using the base rate or Alternative Base Rate in effect on the first business day of the month. Lenders may delay the initial adjustment period. For example, Lenders have used periods as long as 5 years in order to provide the Borrower with an interest rate that is set for the first 5 years of the loan. After that time, the interest rate will begin to fluctuate as stated in the SBA Loan System.

ii. The Lender must specify in the Note the frequency at which the interest rate adjustment will occur.

a) This adjustment period as identified in the Note may not be changed without the written consent of the Borrower.

b) Subsequent adjustments may occur no more frequently than monthly. All subsequent adjustments will set the interest rate on the first calendar day of the adjustment period using the base rate or Alternative Base Rate in effect on the first business day of the adjustment period.

c) The rate of interest will change on the first calendar day of the adjustment period even though the rate may not be known until the second business day of that period.

For example, if the first of the month is a Sunday, the base rate is the Prime rate in effect on Monday. This rate will be reported in the Wall Street Journal on Tuesday, the third calendar day and second business day of the month. Many lenders use the calendar quarter as the adjustment period, especially those that sell the guaranteed portion in the Secondary Market.

iii. After the interest rate begins fluctuating, the loan can be re-amortized. Typically, loans are re-amortized every time the interest rate is adjusted to ensure full amortization by the maturity date.

d. Interest Rate Requirements for an SBA Note:

i. For fixed rate loans, the Lender must state the specific interest rate in the Note.

ii. For variable rate loans, the Lender must include the following information in the Note:

a) Identification of the rate being used as the base rate or Alternative Base Rate;

b) The publication in which the designated base rate appears regularly (e.g., Wall Street Journal from Prime or Treasury Rates, Federal Reserve Bank of New York for SOFR, or the Federal Register if using the SBA Optional Peg Rate). All allowed interest rates are also published on the SBA's website;

c) The percentage spread, including any changes to percentage spread if applicable, to be added to the base rate (e.g., in a construction loan);

d) The initial interest rate of the loan (from disbursement to first adjustment);

e) The date or timing of the first rate adjustment; and

f) The frequency of rate adjustment.

e. Interest Rate Ceilings and Floors:

SBA will permit a Lender to limit the upward and downward adjustments by establishing a floor and ceiling provided that:

i. Both the floor and ceiling are stated in the Note; and

ii. The difference between the stated rate in the Note and the floor is equal to or greater than the difference between the stated rate in the Note and the ceiling.

For example, if the Note rate is 10% and the ceiling is 12%, the floor must be 8% or lower.

f. Accrual Method:

SBA does not require a specific accrual method, unless the loan is sold in the Secondary Market. Loans sold on the Secondary Market must either use 30/360 or Actual/365 as the interest accrual methods. While the interest accrual method 365/360 is permitted on loans not sold on the Secondary Market, Lenders are cautioned that they cannot use this accrual method and charge the maximum allowable rate of interest because this will result in an Annual Percentage Rate that exceeds SBA's regulatory maximum.

g. Amortization: (13 CFR § 120.214(e)):

Lender should use an amortization schedule that is appropriate for the type of loan. SBA does not allow balloon payments. A fixed interest rate loan must use a payment that will fully amortize the loan by the maturity date. Typically, variable rate loans are re-amortized every time the interest rate is adjusted to ensure full amortization by the maturity date. The amortization schedule may also be adjusted to meet the cash flow needs of the business.

4. Fixed and Variable Rate Combinations:

The Lender may use a fixed rate on either the guaranteed or unguaranteed portion and a variable rate on the other portion of the loan. SBA allows such combinations as long as neither rate exceeds the SBA maximum interest rate. A Lender may use this structure to make a loan that permits it to retain a variable interest rate on the unguaranteed portion and sell a fixed rate guaranteed portion on the secondary market. If the Lender uses a combination, the entire loan is considered to be a variable interest rate loan. The interest rate on both the guaranteed and unguaranteed portions must be based on the variable rate.

5. Interest Rate Swap Contracts:

a. An interest rate swap is a contract between two parties where one party pays a fee in exchange for an agreement by the other party to pay any interest in excess of an established amount. The contract may last for all or part of the term of the loan. The swap contract only relates to the payment of interest.

Example: A Borrower has a prime plus 2% interest rate on a 7(a) variable rate guaranteed loan. The Borrower could purchase an interest rate swap contract that would set the interest rate at 8%. When the Note rate is lower than the rate paid by the Borrower on the swap contract (8%), the swap seller keeps the extra amount as compensation for the risk that rates will at some point exceed 8%. When the Note rate is higher than the rate paid by the Borrower on the swap contract, the Borrower would continue to pay the fixed rate of 8% and the swap seller would pay the difference above 8% to the Lender. The ability to stabilize the amount of the loan payment each month is the benefit to the Borrower of an interest rate swap contract.

b. In order to use an interest rate swap in the 7(a) program, the interest rate swap contract must meet the following conditions:

   i. The interest rate swap contract is an agreement between the small business Borrower and the Lender or, if the swap seller is not the lender, a third party. SBA is not a party to the interest rate swap contract.

   ii. The interest rate swap contract does not affect the amount of money owed by the Borrower to SBA in the event SBA purchases the guaranty. In the event of a Borrower default, interest will be calculated using the base rate or Alternative Base Rate and spread in the variable interest rate Note, not the swap contract.

   iii. SBA will not be responsible if the swap seller defaults during the life of the contract. The Borrower will be liable for the interest as required in the Note.

   iv. Loans with accompanying interest rate swap contracts may be sold on the Secondary Market. The Lender is still required under the Secondary Market contract (SBA Form 1086) to forward interest and principal pursuant to the original terms of the loan. It is the Lender's responsibility to work with the swap seller to make sure funds are available for submission to the fiscal and transfer agent according to the time schedule in the Form 1086.

   v. The full amount of the principal and interest required under the Note must be reported by the lender on the SBA Form 1502.

   vi. SBA will not review swap contracts for Borrowers or provide guidance on their use. While swap contracts should not have a significant impact on the cost of the loan, SBA will not publish any guidelines on the cost of these contracts.

   vii. The Borrower must sign a statement acknowledging that interest will be calculated at the Note rate if the swap contract is terminated.

   viii. The following statement must be included in the swap contract that is executed by the Borrower and the swap seller: "The Small Business Administration is not a party to this contract and does not guarantee it. In the event SBA is called upon to honor its guaranty to the Lender, the Borrower's debt will be determined by the terms of the Note, including the variable interest rate provision."

   ix. Swap contracts may be used on new or existing loans.

   x. The swap contract does not have to last for the entire length of the loan agreement.

   xi. SBA does not have a standard form for an interest rate swap contract.

   xii. Any fees owed the swap counterparty as a result of the default by the

Borrower will be subordinated to the SBA 7(a) loan.

## B. PROGRAM-SPECIFIC REQUIREMENTS

The following exceptions and additional requirements apply for each loan program. Where a program states "All General Requirements apply," lenders must refer to the General Requirements section of this Appendix for the applicable collateral standards.

1. Standard 7(a) Loans

   All general requirements set forth in the General Requirements section above apply. No additional program-specific exceptions.

2. 7(a) Small Loans

   All general interest rate requirements apply to 7(a) Small Loans with the following notes:

   a. Default Interest Rates:

      i. 7(a) Small loans: Default interest rates are not permitted.

3. SBA Express Loans

   All general interest rate requirements apply to SBA Express Loans with the following exception:

   a. Default Interest Rates: SBA Express loans allow a default interest rate. The default interest rate is a change (increase) in the interest rate charged to the Borrower upon occurrence of a default event. The Lender must use appropriate and commercially reasonable default interest rates consistent with those used for similar non-SBA guaranteed loans.

      i. For SBA Express variable rate loans, the Lender is not required to use the base rate identified above in this Appendix and in 13 CFR § 120.214(c). It may use the same base rate of interest it uses on its similarly-sized non-SBA guaranteed commercial loans, as well as its established change intervals, payment accruals, etc. However, the interest rate throughout the term of the loan may not exceed the maximum allowable 7(a) interest rate. Only term loans may be sold on the Secondary Market. Loans may only be sold on the Secondary Market if the base rate is one of the base rates allowed in 13 CFR § 120.214(c).

4. 7(a) Manufacturers' Access to Revolving Capital (MARC) Loans

   All general interest rate requirements apply to Manufacturers' Access to Revolving Credit (MARC) loans.

5. CAPLines (All Variants)

   All general interest rate requirements apply to all CAPLine variants.

6. Export Express Loans

All general interest rate requirements apply to Export Express Loans with the following exceptions:

a. For variable rate Export Express loans, the Lender is not required to use the base rate identified above in this Appendix and in 13 CFR § 120.214(c). The Lender may use the same base rate of interest it uses on its similarly-sized, non-SBA guaranteed commercial loans, as well as its established change intervals, payment accruals, etc. However, the interest rate throughout the term of the loan may not exceed the maximum allowable Export Express interest rate and the loan may be sold on the Secondary Market only if the base rate is one of the base rates allowed in 13 CFR § 120.214(c).

b. Default Interest Rates: The default interest rate is a change (increase) in the interest rate charged to the Borrower as a result of a failure to meet certain conditions specified in the loan agreement.

   i. A Lender may charge a default interest rate if it does so for its similarly-sized, non-SBA guaranteed commercial loans, as long as the interest rate does not exceed the maximum interest rate permitted for Export Express loans.

   ii. The amount of interest SBA will pay to a Lender following default of an Export Express loan is capped at the maximum interest rates for the Standard 7(a) loan program.

7. Export Working Capital Program (EWCP) Loans

Except as expressly modified below, the general 7(a) interest rate requirements remain as applicable.

a. SBA does not prescribe the interest rates for the EWCP but will monitor these rates for reasonableness. 13 CFR § 120.344(c)

   i. A loan may have a fixed or variable interest rate. The Lender negotiates the interest rate with the Applicant.

   ii. The base rate may be the daily Secured Overnight Financing Rate (SOFR) + 3%, Prime Rate, or SBA's Optional Peg Rate.

   iii. The spread above the base rate as identified in the Note may not be changed during the life of the loan without the written agreement of the Borrower. For further discussion of variable interest rates, see Paragraph A., iii., "Policy on Variable Interest Rates" in this Appendix.

   iv. After approval and prior to final disbursement, Lender must either notify the LGPC of any changes to the Note terms related to the interest rate or make the change through E-Tran Servicing, or successor SBA Loan System. After final disbursement, Lender must either notify the CLSC by email to

FSC.Servicing@sba.gov of any changes to the Note terms related to the interest rate or make the change through E-Tran Servicing, or successor SBA Loan System.

b. Policy on Variable Interest Rates included in the A. General Policy on Interest Rates in this Appendix.

i. Post-Approval Changes to the Interest Rate:

a) Standard Policy: SBA's maximum allowable interest rate applies only to the initial Note rate on a variable rate loan. Subsequent changes in the base rate are not subject to the maximum rate at the time of loan application; however, the maximum spread over the base cannot exceed SBA's stated maximum.

ii. Accrual Method:

SBA does not require a specific accrual method for EWCP loans.

8. International Trade Loans

All general interest rate requirements apply to International Trade (IT) loans and are set forth above.

# APPENDIX 19: 7(A) COLLATERAL REQUIREMENTS

This Appendix consolidates the collateral requirements applicable to 7(a) loan programs. Lenders must apply the General Requirements below to all 7(a) loan programs unless a Program Specific requirement listed in this Appendix provides otherwise.

## A. GENERAL REQUIREMENTS

1. Collateral

   See Section A, Chapter 5, Paragraph A. for guaranty requirements.

   a. **General collateral standard**

      i. In identifying collateral, Lenders must use commercially reasonable and prudent practices that are at least as thorough as those used for similarly sized, non-SBA guaranteed commercial loans. Decisions regarding what collateral must be taken to secure a loan must be based on the circumstances of the individual loan, including loan size, and must meet the minimum requirements set forth in this Appendix.

   b. **Refinance transactions**

      i. When loan proceeds will be used to refinance existing debt, except for trading assets, the SBA guaranteed loan must be secured with at least the same collateral and lien priority as the debt being refinanced. If the debt being refinanced is over collateralized under SBA collateral requirements and the SBA guaranteed loan will remain fully secured, the Lender may release excess collateral. Substitute collateral may be accepted if it is of comparable value and useful life and is acceptable to SBA or to a PLP Lender acting under its PLP authority.

   c. **Adequacy of collateral**

      i. A Lender may not take any action in connection with an SBA-guaranteed loan that establishes a preference in favor of the Lender (13 CFR § 120.411). A Lender must not have a 7(a) loan in a “piggyback” structure.

         a) Piggyback financing exists when one or more lenders provide more than one loan to a single Borrower at or about the same time, for the same or similar purpose, and the SBA-guaranteed loan is secured by a junior lien position or no lien position on the collateral securing the non-SBA loan or loans. Loans approved within 90 days of one another are considered approved at or about the same time.

         b) A structure is not considered piggyback financing when both the SBA-guaranteed loan and the non-SBA loan are for working capital and the

non-SBA loan is secured only by working or trading assets. A pari passu lien position is also not piggyback financing when the maturity of the non-SBA loan is not shorter than the maturity of the SBA-guaranteed loan.

c) A loan request must not be declined solely because collateral is inadequate. SBA recognizes that Applicants may demonstrate repayment ability even when they lack collateral sufficient to repay the loan in full upon default. However, the SBA guaranty is not a substitute for available collateral.

d) When assessing collateral adequacy, the Lender must evaluate the impact of covenants and other recorded restrictions on collateral value and marketability and must document that analysis in the loan file. The review must include, as applicable, deed restrictions, easements, reversionary interests, subordinations, leases, options, engineering controls, and similar restrictions. Environmental indemnification provisions that run with the land are not eligible and must be removed or waived as to the Federal Government.

d. **Real estate appraisal and fixed-asset valuation requirements**

i. When commercial real estate is taken as collateral and an appraisal is required under the applicable loan program section of this Appendix, the appraisal must comply with 13 CFR 120.160(b), be prepared by an independent State-licensed or State-certified appraiser, be USPAP compliant, and be dated within 12 months of the application for guaranty.

ii. The appraiser must be independent of the loan production function, must not be involved in approval of the transaction, and must not have the appearance of a conflict of interest. If the estimated value of the commercial property exceeds $1,000,000, the appraiser must be State-certified.

iii. The appraisal must identify the Lender as the client and/or intended user, except to the extent a federally regulated Lender may follow applicable FIRREA requirements. The Lender may not use an appraisal prepared for the seller or Applicant.

iv. If the valuation of fixed assets exceeds Net Book Value, the Lender must obtain an independent appraisal by a qualified individual to support the higher valuation. The appraiser must be independent of the loan production function, not involved in the credit approval decision, and free of any apparent conflict of interest.

v. SBA has no specific appraisal requirements for non-commercial real estate taken to secure a personal guaranty unless a program-specific section of this Appendix states otherwise.

e. **Change of ownership valuation requirements**

i. When loan proceeds will finance a change of ownership, the Lender must comply with the business valuation and appraisal requirements applicable to change of ownership transactions in Appendix 15 7(a) Changes of Ownership, including any required independent valuation thresholds, special purpose property requirements, and lender verification of financial information used in the valuation.

## B. PROGRAM-SPECIFIC REQUIREMENTS

The following exceptions and additional requirements apply for each loan program. Where a program states "All General Requirements apply," lenders must refer to the General Requirements section of this Appendix for the applicable collateral standards.

1. Standard 7(a) Loans

a. All General Requirements in this Appendix apply to Standard 7(a) Loans. In addition, the following collateral rules are unique to Standard 7(a) Loans:

b. A Standard 7(a) Loan is fully secured when the Lender has taken security interests in all available fixed assets of the Applicant, using the valuation limits set forth in this Appendix, up to the loan amount.

i. If there is a collateral shortfall, the Lender must take available equity in personal real estate (residential and investment property including other commercial real estate regardless of whether the owner is actively running a business at the investment property) that is solely owned by any Co-Borrowers, direct or indirect owners of 20 percent or more of the Applicant, and/or guarantors, except Supplemental Guarantors, subject to the limitations described in this Appendix. For purposes of this requirement, “solely owned” real estate includes property held in an entity that is solely owned, directly or indirectly, by such persons. Liens on personal real estate may be limited to the amount of the collateral shortfall. In addition, liens on personal real estate may be limited to 150% of the equity in the collateral.

ii. The Lender is not required to take real estate collateral to satisfy the fully secured test when the equity in the real estate is less than 25 percent of fair market value, but the Lender must document that determination from a source other than the personal financial statement.

c. When loan proceeds are used to acquire, refinance, or improve assets, the Lender must obtain a first lien on those assets, except where this Appendix permits a subordinate lien for asset improvements or does not require a lien on certain vehicles.

d. When an individual alone or together with a spouse or minor children owns 20

percent or more of the Applicant, the Lender must consider liens on qualifying personal real estate owned individually or jointly with that spouse or minor children. Transfers to a non-owning spouse or minor children within 6 months of application are not exempt from collateral consideration.

e. For loans collateralized by commercial real estate, the Lender must obtain an appraisal that complies with the real estate appraisal requirements in this Appendix and the applicable environmental requirements.

2. 7(a) Small Loans

a. All General Requirements in this Appendix apply to 7(a) Small Loans except as modified below.

b. 7(a) Small Loans of $50,000 or less

i. For 7(a) Small Loans of $50,000 or less, collateral is not required. Lenders may, but are not required to, take additional collateral consistent with their own policies and procedures.

c. 7(a) Small Loans greater than $50,000 – required collateral

i. General Rule:

a) For 7(a) Small Loans greater than $50,000, the Lender must, at a minimum, take a first lien on assets financed with loan proceeds, except where this Appendix does not require a lien on certain vehicles or permits a subordinate lien for improvements to existing assets.

ii. Working Capital:

When 50 percent or more of the loan proceeds will be used for working capital, the Lender must take a lien on all fixed assets of the Applicant business, including real estate, up to the point the loan is fully secured, using the valuation limits set forth in this Appendix. SBA considers a loan “fully secured” when the Lender has taken security interests in all available fixed assets of the Applicant business with a combined Net Book Value, as adjusted in this Appendix, up to the loan amount. For 7(a) loans, “fixed assets” means real estate (including land and structures) and machinery and equipment owned by the Applicant business or EPC.

The Lender is not required to take a lien on Applicant business real estate when equity is less than 25 percent of fair market value, and may limit the lien to the amount necessary to fully secure the loan. Improved real estate may be valued at no more than 85 percent and unimproved real estate at no more than 50 percent of market value for calculating whether the loan is fully secured, and such values must be determined in accordance with the real

estate appraisal and fixed asset valuation requirements in Paragraph A.1.d. of this Appendix.

iii. Refinancing existing debt

a) When proceeds of a 7(a) Small Loan will be used to refinance existing debt, the loan must be secured with at least the same collateral and lien priority as the debt being refinanced. If the debt being refinanced is over-collateralized under SBA collateral requirements and the 7(a) Small Loan will remain fully secured after release, the Lender may approve the release of excess collateral. Substitute collateral may be offered if it is of comparable value and useful life and is determined acceptable by SBA or by a PLP Lender processing the loan under its PLP authority.

d. Additional collateral lenders may choose to take

i. For 7(a) Small Loans, SBA only requires the collateral described in Paragraph 1., b-1.c. However, SBA does not prohibit a Lender, consistent with its own policies and procedures, from taking additional collateral, including but not limited to:

a) Available equity in personal real estate (residential and investment property) of any owners and guarantors.

b) Trading assets of the Applicant business.

c) Commercial, residential, or investment real estate owned by the Applicant or personally by the owners or guarantors.

3. SBA Express Loans

a. All General Requirements in this Appendix apply to SBA Express Loans except as modified below.

b. For SBA Express Loans of $50,000 or less, collateral is not required.

c. For SBA Express Loans greater than $50,000, the Lender must follow the General Requirements in this Appendix but may use its own collateral policies and procedures for similarly sized, non-SBA guaranteed commercial loans in place of SBA's detailed collateral procedures, unless another SBA Express-specific requirement applies.

4. 7(a) Manufacturers' Access to Revolving Capital (MARC) Loans

a. All General Requirements in this Appendix apply to 7(a) MARC Loans except as modified below.

b. The Lender must place a lien on all assets of the business through a UCC-1 filing.

i. The Lender must obtain a first lien on the trading assets of the business,

including accounts receivable and inventory.

5. CAPLines

All General Requirements in this Appendix apply to all CAPLines unless a variant-specific requirement below states otherwise.

**a. General CAPLines rules**

i. For CAPLines of $50,000 or less, collateral is not required.

ii. For Working Capital CAPLines that refinance existing debt, the line should be secured with at least the same collateral and lien priority as the debt being refinanced. If the refinanced debt is over collateralized under SBA standards and the line will remain fully secured, the Lender is not required to take excess collateral. Substitute collateral may be accepted if it is of comparable value and useful life and is acceptable to SBA or to a PLP Lender acting under its PLP authority.

**b. Working Capital CAPLines**

i. If the Lender will disburse the line based on a borrowing base certificate, the Lender must obtain a first lien on the Applicant's working or trading assets, including accounts receivable and inventory.

a) If the Lender will not use a borrowing base certificate, the Lender must assume full use of the line and secure the line with sufficient collateral to ensure a 1:1 collateral ratio. The Lender must obtain a first lien on working or trading assets and must take additional collateral if needed to maintain the required ratio.

b) If business assets do not fully secure the line, the Lender must take available equity in personal real estate of owners of 20 percent or more of the Applicant and guarantors, except Supplemental Guarantors, subject to the limitations stated in this Appendix, including the rule that real estate with less than 25 percent equity need not be pledged.

**c. Contract CAPLines**

i. The Applicant must provide the Lender with a first lien position on the contract or contracts financed and on the proceeds of those contracts, by assignment and appropriate UCC filing, except where an assignment exception in this SOP applies.

ii. The Lender may take additional collateral in accordance with its policies and procedures for similarly sized non-SBA guaranteed commercial lines of credit.

iii. All liens must be perfected and lien position verified before the initial disbursement, and for revolving structures that cover more than one season,

contract, or project, before each relevant disbursement cycle.

**d. Builders CAPLines**

i. SBA will accept no less than a second lien position on the property being constructed or renovated if the purpose of the first lien was to acquire the property.

ii. If the property is part of a subdivision or secures a loan with more than one parcel, the first lienholder must provide a release clause that permits transfer of clear title to an eventual buyer upon receipt of a pre-established payment.

iii. The Lender must not take a second lien position if the first lienholder requires full payoff of the entire first loan before any parcel will be released. If the Lender and SBA are in second position, the total amount needed to release the first and second liens may not exceed 80 percent of the fair market value of the completed project.

6. Export Express Loans

   a. All General Requirements in this Appendix apply to Export Express Loans except as modified below.

   b. For Export Express Loans of $50,000 or less, collateral is not required.

   c. For Export Express Loans greater than $50,000, the Lender must follow its own written collateral policies and procedures for similarly sized, non-SBA guaranteed commercial loans, except as otherwise required for standby letters of credit or other Export Express specific structures.

   d. For an Export Express line of credit over $50,000 that supports a standby letter of credit, the line must be collateralized to provide at least 25 percent coverage of the standby letter of credit amount through cash, cash equivalents, or project collateral.

7. Export Working Capital Program (EWCP) Loans

   a. All General Requirements in this Appendix apply to EWCP Loans except as modified below.

   b. The Lender must obtain no less than a first security interest in all collateral associated with the financed export transaction or transactions, including export-related inventory, receivables, credit insurance assignments, letters of credit proceeds, and contract proceeds, to the extent required by program rules.

   c. The Lender must manage the facility so that the loan remains in margin at all times under applicable EWCP borrowing base requirements, and SBA or a PLP-EWCP Lender may require additional collateral to maintain that position.

   d. When EWCP proceeds refinance debt, the collateral securing the debt being

refinanced must be transferred to the EWCP loan. If EWCP is provided together with a term loan, the EWCP loan must have lien priority on the trading assets that secure the EWCP facility.

e. Standby letter of credit structures under EWCP must comply with the collateral coverage, reserve, and liquidation requirements applicable to that program.

In general, the export-related inventory produced, and the foreign accounts receivables generated by the business will be considered to provide adequate collateral coverage, and the Lender must take active steps to ensure that the loan always remains in margin. SBA considers a loan to be "In Margin" when the loan availability established per the EWCP formula is equal to or greater than the principal balance. SBA, for non-delegated loans, or the PLP-EWCP Lender for loans processed under delegated authority, may require additional collateral by requiring a lien on other business assets.

When EWCP loan proceeds are used for debt refinancing, collateral for the loan being refinanced must be transferred to secure the EWCP loan.

An EWCP loan may be issued at the same time as a term loan (conventional or SBA-guaranteed). When doing so, the EWCP loan must have lien priority on the trading assets securing and being used by the EWCP loan. The Lender must clearly identify the assets securing the EWCP loan in the credit memo.

i. Standby Letters of Credit: Lenders are required to obtain and maintain sufficient collateral if an EWCP loan is used to support the issuance of a Standby Letter of Credit. Under a Transaction-Based loan, the Applicant must deposit cash into an account held by the Lender in an amount equal to at least 25% of the standby letter of credit being issued. This deposit must remain in the account held by the Lender for the term of the standby letter of credit. If using an asset-based loan (ABL) facility, SBA, for non-delegated loans, or the PLP-EWCP Lender may allow export inventory and/or foreign accounts receivable or other acceptable collateral to replace the cash deposit requirement. The Lender must determine that the borrowing base for the ABL will support at least 25% of the total of all standby letters of credit supported by the loan. All Lenders must document the method used to secure the additional collateral in their file.

a) Standby Letters of Credit can be issued to support either performance or financial needs of the Borrower,

b) When issuing a financial standby letter of credit under an Asset-Based EWCP loan, the Lender must fully secure the obligation at 100% collateral against borrowing base availability.

c) When issuing either a performance or financial standby letter of credit, the Lender must reserve 100% of the amount issued against the gross

amount of the EWCP loan. This is to ensure that the facility has enough capacity to fund a draw on the letter of credit.

d) Lenders using a cash deposit to satisfy the EWCP 25% collateral requirement for performance letters of credit may elect to reserve 75% of the issued letter of credit amount given the liquid nature of the deposit being held.

e) In the event of a draw on the standby letter of credit, the Lender must liquidate the cash held on deposit or release the BBC collateral hold.

ii. Receivables generated from sales to foreign purchasers are not considered a foreign asset and may be taken as collateral.

iii. Personal guaranties of all 20% or more owners is generally required, but may be waived by the Director, International Trade Finance (D/ITF).

8. International Trade (IT) Loans

a. All General Requirements in this Appendix apply to International Trade Loans except as modified below.

b. Required Lien Position

The Small Business Act, Section 7(a)(16)(B), requires that the Lender take a first lien on the assets financed with IT loan proceeds or other assets of the Applicant. A Lender may request a policy exception from the Director of Financial Assistance (D/FA) if it wishes to make an IT loan that is not in first position on the assets financed, provided the second lien provides adequate assurance of repayment of the loan.

c. For example, when the IT loan is to improve business real estate (such as financing an addition to an existing building), and the collateral securing the IT loan is subject to a first lien securing an existing loan used to acquire the business real estate or equipment, the Lender may request a policy exception for the IT loan. SBA Lenders may request this policy exception via email at 7adelegatedloanapps@sba.govAdequacy of Collateral:

i. When assessing the adequacy of collateral, the Lender must consider the impact that covenants and other restrictions recorded against the collateral may have on its value and marketability. The Lender must document this analysis in the file. Examples of items to review include:

a) Deed restrictions, covenants, easement provisions, reversionary interests, subordinations, leases and options, and other provisions that restrict the use of the property for the benefit of a third party (note: certain deed restrictions pertaining to the use of the property, which are intended to protect the health and safety of occupants, may be acceptable, e.g., deed restrictions based upon environmental concerns

including restrictions on residential use, use as a day care center for children or seniors, use as a school, or use as a hospital); and

b) Engineering Controls that require the Applicant or subsequent owners to install costly devices or structures such as extraction wells or subsurface barrier walls prior to constructing a building, remodeling, or otherwise improving the property. Each IT loan must be secured either by a first lien position or first mortgage on the property or equipment financed by the IT loan or on other assets of the Borrower, except that an IT loan may be secured by a second lien position on the property or equipment financed by the IT loan or on other assets of the Borrower, if the SBA determines the second lien position provides adequate assurance of the payment of the IT loan.

c) Environmental Indemnification provisions that run with the land are not eligible and need to be removed or waived as to the Federal Government.

d. For all loans that are collateralized by commercial real estate, Lenders must comply with the requirements for real estate appraisals or evaluations as stated in the general collateral requirements in this Appendix. .

# APPENDIX 20: SUBMISSION OF APPLICATION FOR GUARANTY

This Appendix consolidates the contents of the lender's application for guaranty requirements applicable to all 7(a) loan programs. Lenders must satisfy the General Requirements below for all 7(a) loans. The Program-Specific Requirements section lists only the exceptions, modifications, or additional documentation requirements that differ from the General Requirements for each loan program.

## A. GENERAL REQUIREMENTS

1. Contents of Lender's Application for Guaranty & Submission to SBA

   Regardless of the processing method, all 7(a) loan files must include the forms and information the Lender requires in order to make an informed credit decision. Program forms can be found at www.sba.gov/document. Centralized 7(a) Loan Submission Instructions can be found at the 7(a) Loan Guaranty Processing Center ("LGPC") website at Loan Guaranty Processing Center (Citrus Heights, CA and Hazard, KY) | U.S. Small Business Administration.

   Lender must submit to the SBA Loan System all terms and conditions required by the SBA Loan System data fields.

   Lender must list in the SBA Loan System 100% of the total direct and indirect ownership of the Applicant. The ownership percentages of all listed owners must equal 100%.

   SBA Form 1919 includes information on the number of existing employees at the time of application and the number of jobs to be created and/or retained as a result of the loan.

   - Number of existing employees at the time of application is calculated in accordance with 13 CFR § 121.106, which states in part that SBA counts all individuals employed on a full-time, part-time, or other basis (i.e., jobs are not converted to full-time equivalents).
   - Jobs "created" means the number of full-time (or equivalent) employees that the small business expects to hire as a result of the loan.
   - Jobs "retained" means the number of full-time (or equivalent) employees on the payroll of the business at the time of application that will be lost if the loan is not approved.
   - "Employees" does not include contractors reported via IRS Form 1099.

   **For all loans submitted using the Lender's PLP delegated authority**, Lender must submit the information required in SBA Form 1919 and the loan terms and conditions into the SBA Loan System. The Lender must obtain and retain in its file all documentation listed below.

   **For all loans submitted using the non-delegated process through the LGPC**, the Lender must submit applications for guaranty and all attachments via the SBA Loan

System to SBA. SBA will make the final determination as to the eligibility and creditworthiness of the Applicant, including approving the uses of proceeds, the adequacy of the collateral being pledged, the structure of the loan, and any equity contribution to be required from the Applicant. SBA will either approve or decline the loan in the SBA Loan System. The Lender must obtain and retain in its file all documentation listed below. **In addition, Lender must submit as part of the application for guaranty those items below emphasized in bold**.

a. SBA Form 1919: A separate SBA Form 1919 for each Co-Borrower must be completed and signed by the authorized representative of the Applicant and submitted to the Lender. The aggregate amounts of the "Purpose of the loan" sections across all SBA Forms 1919 should equal the total amount of the loan request. Only the information required on SBA Form 1919, and not the form itself, must be submitted into the SBA Loan System, although the Lender must obtain and retain the signed form in its file.

b. **Lender's Credit Memorandum** must address all requirements detailed in the Credit Standards Paragraph for the applicable loan program Chapter.

c. **Owner Financial Statement** for all owners of 20% or more (including the assets of the owner's spouse and minor children), and proposed guarantors, except Supplemental Guarantors, Lenders may use SBA Form 413 or their own equivalent form signed and dated within 90 days of submission to SBA. Business financial statements must be dated within 120 days of submission to SBA.

d. Tax transcripts in accordance with Section A, Ch. 5, Para. B, IRS Tax Transcript/ Verification of Financial Information and either **business financial statements or tax returns for the last 3 years and interim financial statements for the Applicant and any affiliates. For start-ups, new businesses, changes of ownership, and other applications based on projections, include detailed projections, including the supporting assumptions that reflect a debt service coverage equal to or greater than 1.15 within 2 years from loan funding or, for construction projects, within 2 years from the end of construction**. Interim financial statements must be dated within 120 days prior to submission to SBA. The following information must be provided:

   i. Year End Balance Sheet for the last 3 years, including detailed debt schedule;

   ii. Year End Profit & Loss Statements for the last 3 years;

   iii. Interim Balance Sheet, including a detailed debt schedule, and interim Profit & Loss Statements.

e. Copy of Lease, if applicable;

f. Detailed listing of machinery and equipment to be purchased with loan proceeds and cost quotes, if applicable;

g. A detailed listing of all assets purchased with loan proceeds;

h. A detailed listing of all collateral;

i. Franchise: For any Applicant operating under a franchise, license or similar agreement, refer to Section A, Ch. 1, Para. G., "Franchises".

j. Provide the following if real estate is to be purchased with loan proceeds:

   i. Appraisal (See appraisal requirements in Appendix 19 Para. A.1.d. Real estate appraisal and fixed asset valuation requirements;

   ii. **Copy of signed purchase agreement**;

   iii. Lender's environmental questionnaire (if applicable – see Section A, Ch. 5, Para. E, Environmental Policies and Procedures); and

   iv. **Cost breakdown** where improvements to the real estate are included;

k. Provide the following if purchasing an existing business with loan proceeds:

   i. **Copy of buy-sell agreement**;

   ii. **Copy of business valuation** that meets the requirements in Appendix 15 Para. C.1.a. Business Valuation Requirements - Change of Ownership;

   iii. **Pro forma balance sheet** for the business being purchased as of the date of transfer;

   iv. **Copy of seller's financial statements** for the last 3 complete fiscal years or for the number of years in business if less than 3 years. The financial statements must be dated and either signed or certified by the seller within 120 days prior to submission to SBA; and

   v. **Seller's interim financial statements** no older than 120 days from date of submission to SBA. The financial statements must be dated and either signed or certified by the seller. If seller's financial statements are not available, the seller must provide an alternate source of verifying revenues. If seller's financial statements are not available, Lender must discuss in its credit analysis:

      a) Why financial statements are not available; and

      b) How the Lender verified business revenue.

l. **Debt Refinancing**. Lenders must maintain copies of all notes being refinanced, security agreements, leases, transcripts for the most recent 12 months (to prove debt being refinanced is current) or other documentation evidencing the debt to be refinanced in the loan file. For non-delegated loans, Lender must submit copies of all these documents for the debt to be refinanced to the LGPC with the application.

m. **Documentation of U.S. National** in accordance with Section A, Ch. 1, Para. F., "Citizenship and Residency Requirements". Lenders must receive verification of

the status of each U.S. National. Lender must document their findings of the review proving a U.S. National's status (birth certificate and/or passport) in the loan file, and enter the U.S. National's Social Security Number on the Application in the SBA Loan System.

n. Management agreements, if applicable, and if the management agreement is not part of the franchise disclosure documents for a brand listed on the Franchise Directory. See Section A, Ch. 1, Para. E.3.e. on management agreements.

2. Where to Submit Applications for Guaranty

   a. Non-delegated applications – Lenders submitting applications using non-delegated procedures must submit applications for guaranty and all attachments via the SBA Loan System to the LGPC. *Documents greater than 250MB must be separated into multiple documents. The system does not support uploads greater than 250MB.*

   b. PLP applications – Lenders submitting applications using their PLP authority must submit guaranty applications via the SBA Loan System, retaining all required documentation in the Lender's loan file.

   c. Reconsideration of Declined non-delegated Standard 7(a) Loan Applications (13 CFR § 120.193):

      i. If the Lender believes the reason(s) for decline have been overcome, a request for reconsideration may be submitted along with a detailed written explanation of how the Applicant has overcome the reason(s) for decline. Lender must submit a request for reconsideration to the LGPC within 6 months of the date of decline. Any request submitted more than 120 days after the date of decline must include current financial statements.

      ii. If a request for reconsideration is declined by the LGPC, a second reconsideration may be requested from the D/FA or designee, whose decision is final. The request to the D/FA or designee must be submitted to the LGPC and must include a copy of the Center's decline letter and include additional information that specifically addresses the reason(s) identified for decline and how the Applicant has overcome those reason(s). The LGPC will forward the request to the D/FA or designee for a final decision.

3. See Chapter 6, SBA Terms and Conditions through Disbursement for all 7(a) Loans, in Section B, for SBA requirements for the SBA Terms and Conditions, post-approval and pre-disbursement requests for changes, transfer of guaranty between participating Lenders, and loan closing and disbursement.

**B. PROGRAM SPECIFIC REQUIREMENTS:**

The following exceptions, modifications, and additional documentation requirements apply for each loan program. Unless otherwise noted below, all General Requirements in this Appendix apply.

1. Standard 7(a) Loans, 7(a) Small Loans, Express, Export Express and MARC Loans:
    a. All general requirements set forth in the General Requirements section above apply. No additional program-specific exceptions.
2. CAPLines-Specific Loan Closing and Disbursement Requirements

    See Section B, Ch. 6, Para. D for additional requirements for loan closing and disbursement.

    a. Seasonal CAPLines:
        i. Disbursement and Repayment:
            a) Disbursements from the loan are made continually during the seasonal build-up period when the cash requirement for labor, materials, and support of accounts receivables exceeds actual cash receipts. The final disbursement of any Seasonal loan should be made in time for the funds to be used in the business and converted to cash which can be used to pay off the loan balance at the commencement of a 30 day clean up period or maturity.
            b) Principal repayments on the loan must occur as soon as the cash from the seasonal sales has been received by the Borrower. Interest should be paid monthly.
        ii. Borrowing Base Certificate (BBC):

            Lender may use BBCs to monitor the Borrower's seasonal activity. If the Lender does so, the BBC must be submitted by the Borrower to the Lender no less frequently than monthly.

    b. Contract CAPLines:
        i. Assignment of Contract Proceeds:
            a) Subject to the exception noted in b) below, prior to initial disbursement on any Contract CAPLine, the entity the Borrower has entered into the contract with must be advised in writing by both the Lender and Borrower that an assignment of the contract proceeds is required. Such assignment must be in place before any disbursement for a particular contract is made and include a provision for the Lender's right to receive all payments from the third party. The Lender must receive written acknowledgement from the third party.

b) Exception to the Assignment of Contract Proceeds: An assignment of the contract proceeds may be foregone, if at least two of the following conditions are met:

i) The term of the contract being financed is 12 months or less;

ii) A successful track record between the Borrower and the contracting authority exists relative to the same or reasonably similar contracts. (The definition of a "successful track record" includes but is not limited to, any prior contractual arrangement between the subject parties, where the responsibilities of each party under the contract were met to the satisfaction of all parties to the contract.);

iii) Financial analysis of historical income statements and/or tax returns and pro-forma financial statements show that the applicant has a Debt Service Coverage ratio that exceeds 1:1;

iv) All contract proceeds are paid directly to the lender by the contracting authority or, in the instance where a performance bond is in place, a Funds Control (or escrow or third party servicer) procedure is implemented; or

v) There is other available and worthwhile collateral pledged to secure the line by either the Borrower or any owner/guarantor, except Supplemental Guarantors.

ii. Prime and Subcontractor Contracts:

Subject to Subparagraph 3.b.i., Assignment of Contract Proceeds, above, a contract between a Prime and Subcontractor is eligible to be financed with a Contract CAPLine, if at least two of the following conditions are met:

a) Both the Prime and the Subcontractor have favorable credit ratings based on an acceptable rating agency (e.g., Builders Industry Credit Association "BICA");

b) There is a successful track record between the Prime contractor and the Subcontractor (Borrower);

c) There is a successful track record between the Prime contractor and the contracting authority;

d) The Contract CAPLine amount is less than $300,000;

e) The term of the contract is 12 months or less;

f) The financial analysis of historical income statements and/or tax returns and pro-forma financial statements show that the applicant has a Debt Service Coverage ratio that exceeds 1:1; or

g) There is other available and worthwhile collateral pledged by either the Borrower or any owner/guarantor, except Supplemental Guarantors.

iii. Contracts with Performance Bonds:

Subject to Subparagraph 3.b.i, Assignment of Contract Proceeds, above, a contract requiring a Surety's performance bond may be eligible for a Contract CAPLine provided the Lender perfects a UCC security interest in the contract proceeds.

SBA recognizes the following conditions may be necessary to effectuate the transaction where a contract requires a Surety's performance bond:

a) The Lender's perfected UCC security interest in the contract proceeds will be subordinate to the cost reimbursement claim of the Surety; and

b) The Surety may require that a funds control facility be executed. The funds control facility would disburse directly to suppliers and laborers. The contracting authority will remit contract proceeds directly to the funds control facility, which will remit payment to the lender.

iv. Purchase Orders under a Master Agreement:

Purchase Orders (PO) may be substituted for a formal contract, provided the following conditions exist:

a) The PO is issued to the Borrower under a Master Agreement; and

b) The combination of the PO and the Master Agreement constitute a binding agreement.

v. Disbursements are made, when needed, to pay for the costs on a specific contract. Disbursements will generally be made as the contract progresses, not with one lump sum disbursement to cover all costs. Only if the contract performance period was 30 days or less should only one disbursement for payroll be allowed. However, if a borrowing contractor wanted to acquire all of their materials up front to take advantage of volume discounts, and/or pay for all acquired materials within 10 days to take advantage of prompt pay discounts, the Contract CAPLine Program will accommodate such a disbursement plan.

vi. With the assignment of contract proceeds and direct payment in place, the Lender receives all the payments the Borrower would normally receive if it was internally financing the contract as performance progresses. Because all performance costs (including direct overhead and allocated general/ administrative expenses) were funded under the CAPLine, all such payments received by the Lender must be applied first to interest due on the CAPLine, with the remainder applied to the CAPLine balance until the balance is paid in full.

vii. If deemed necessary from a credit standpoint by the Lender, the Lender may invoke additional controls over the payments, provided the Lender obtains the Borrower's prior written consent. If such additional controls include the funding of direct material and labor only, as opposed to all contract costs, then the Lender must inform the Borrower in writing of the percentage split arrangement regarding the allocation of progress payments received from the contracting authority.

c. Builders CAPLines:

i. Prior to disbursement for each individual project, the lien must be recorded and position verified. Interim disbursements shall be made as construction progresses at stages approved by Lender, but shall be advanced only on qualified architect, appraiser or engineer's certification and personal inspection by proper Lender officer(s). Amount of disbursement shall not exceed 100% of labor, material, and other eligible costs of construction certified to be complete and shall be supported by contractor's statements and lien waivers to date.

ii. Prior to final disbursement of construction funds, final lien waivers must be obtained from Borrower/contractor and all subcontractors, material men, and any independent workers involved in the construction. No disbursement can be made after maturity of the master note.

iii. The repayment of all funds disbursed for any individual project shall occur within 36 months after completion of each individual project or at the time of sale, whichever is less. A single principal payment is acceptable. Interest payments must be made at least semi-annually and from the applicant's own resources, not from loan proceeds.

d. Working Capital CAPLines:

i. For Working Capital CAPLines, Lenders have the option of disbursing the line loan proceeds based on a BBC, or 1:1 collateral ratio when the loan is less than $2,000,000. For Working Capital CAPLines equal to or greater than $2,000,000, loan proceeds must be administered through a BBC.

a) If a Lender will not use a BBC to determine the availability of funds for disbursement, the Lender must:

i) Use a combination of factors for the underwriting and credit decision consistent with its similarly-sized, non-SBA guaranteed commercial lines of credit, including at a minimum;

(a) Cash flow analysis to determine the adequacy, duration, and dependability of cash flow;

(b) Collateral analysis to establish an estimated value of collateral; and

(c) Owner/Guarantor analysis, except Supplemental Guarantors;

ii) Assume full utilization of the revolving line of credit and secure the line with sufficient collateral to ensure there is a 1:1 collateral ratio. Lender must obtain a first lien position on the working/trading assets (accounts receivable and inventory) financed with the line. If the working/trading assets are insufficient to provide a 1:1 collateral ratio, the Lender also must take additional collateral to ensure there is a 1:1 collateral ratio. If business assets do not fully secure the line, the Lender must take available personal equity in personal real estate of the principals as collateral to ensure there is a 1:1 collateral ratio;

(a) To determine if there is a 1:1 collateral ratio, discount the available collateral based upon the Net Book Value presented on the Borrower's financial statements. The total line amount should be supported with accounts receivable at a maximum of 80% (after discounting a percentage for any ineligible receivables identified by reviewing the accounts receivable aging) and inventory no greater than 50%. Machinery and equipment may be valued at 50% of Net Book Value or 80% with an Orderly Liquidation Value minus any prior liens. Real estate can be supported at 85% of the value;

(b) If the line will be secured by fixed assets and the valuation of fixed assets is greater than their Net Book Value, an independent appraisal by a qualified individual must be obtained by the lender to support the higher valuation. The appraiser must be independent of the loan production function, not involved in the approval of the transaction, and must not have the appearance of a conflict of interest;

iii) Obtain Borrower prepared financial statements and tax returns if the CAPLine amount is $1,000,000 or less and compiled, reviewed, or audited financial statements and tax returns if the CAPLine amount is over $1,000,000, consistent with lender's policies governing its similarly-sized, non-SBA guaranteed commercial lines of credit;

iv) Use financial covenants consistent with those used on Lender's similarly-sized, non-SBA guaranteed commercial lines of credit. These balance sheet covenants such as a Current Ratio or Debt to Tangible Net Worth ratio should be tested quarterly, semi-annually, or annually, consistent with Lender's policies governing its similarly-sized, non-SBA guaranteed commercial lines of credit; and

v) Monitor the lines consistent with the Lender's policies and procedures for its similarly-sized, non-SBA guaranteed commercial lines of credit and, at a minimum, conduct a credit review including cash flow

analysis, collateral analysis to ensure there is a 1:1 collateral ratio, owner/guarantor (except Supplemental Guarantors) credit review and site visit on an annual basis.

vi) Proceeds from cash sales and receivable collections must pay down the line as collected consistent with Borrowers operating cash cycle.

vii) If required, Lenders must report the initial disbursement consistent with their similarly-sized, non-SBA guaranteed commercial loans in accordance with Section B, Ch. 6, Para. D.4.c., Additional required documents include:.

b) If the Lender will use a BBC to determine the availability of funds for disbursement the lender must adhere to the following:

i) Loan proceeds may be disbursed to the Borrower's operating account. To calculate the maximum amount available for disbursement, use the following formula:

| | |
|---|---|
| Eligible A/R | $ |
| Multiplied by advance rate (multiplied by) | % |
| Equals **A/R Borrowing Base** (BB) = | $ |
| Eligible inventory | $ |
| Multiplied by advance rate (multiplied by) | % |
| Equals **Inventory BB** = | $ |
| **Total A/R & Inventory BB:** (A/R BB + Inventory BB) | $ |
| Face amount of Note | $ |
| Borrowing base (Lesser of Total A/R & Inv BB or Note) | $ |
| Subtract loan balance on books (minus) | $ |
| Equals **Amount available for disbursement** | $ |

ii) No less than monthly, Lender should determine the amount of eligible assets for the borrowing base.

(a) When advancing against receivables, Lender should:

(i) Obtain an aging of accounts receivable and accounts payable;

(ii) Eliminate all ineligible receivables. The following types of accounts are not eligible to be included in the borrowing base:

*(a)* Any invoice more than 90 days past due. Exceptions are permitted over the 90 day with SBA's prior written

concurrence. To avoid unnecessary disqualification of receivables, the Borrower may structure their receivables terms so that the due date properly reflects the cash conversion cycle (timely payment) of the customer.

*(b)* If a customer is delinquent on more than 50% of its total outstanding invoices, ALL of the accounts due from that customer are ineligible. To re-establish the customer's accounts as eligible, all delinquent accounts must be paid in full. Exceptions are permitted if the Lender obtains SBA's prior written concurrence.

*(c)* All re-billed accounts. (Re-billing is the practice of issuing a credit to a customer and re-invoicing the obligation in the current billing cycle. If the re-billing occurs on the same day in order to correct a clerical error, the accounts do not have to be excluded.)

*(d)* Foreign receivables not backed by documentary or standby letters of credit, factor's guarantee (of purchase), credit insurance (either commercial risk or commercial and political risk combinations), or Government enhancements such as those provided by the Export Import Bank or the World Bank.

*(e)* Offsetting receivables and payables between the Borrower and one of its creditors (contra accounts).

*(f)* Accounts due from affiliate companies.

*(g)* Accounts that require subordination to other parties, such as Governmental contracts where the bonding company requires assignment of the project's receivables.

(b) When advancing against inventory, a Lender should:

(i) Obtain a description of inventory and its value; and

(ii) Limit advances to the following types of inventory:

*(a)* Finished Goods: Eligible if readily saleable and not obsolete.

*(b)* Work in Progress: Eligible if Lender obtains SBA's prior written concurrence.

*(c)* Commodities or Raw Materials: Eligible.

(c) The dollar amount of ineligible receivables and inventory will remain unchanged for the entire month. The actual borrowing availability may increase or decrease as the balance on the line

changes and the receivables and inventory are generated or converted back to cash.

(d) A BBC is required at least monthly to determine the amount that can be disbursed. Lender may require a BBC more frequently consistent with its policy and procedures on similarly-sized non-SBA guaranteed commercial lines of credit. Lenders may use their own forms for the BBC.

iii) Repayments will come from cash sales and receivable collections. Proceeds must pay down the line as collected with availability to re-advance as long as the Borrower is conforming to the maximum amount of the BBC.

iv) If a cash collateral account is being used and a balance remains in the cash collateral account after the loan has been paid down to zero, those funds may be credited to Borrower's operating account. There is no provision for interest only payments. Interest must be paid at least monthly either from Borrower's own resources OR from loan proceeds at the time of an advance. Principal payments should be tied to the Borrower's cash cycle.

v) Lenders must report the initial disbursement on SBA Form 1050 or Lender equivalent in accordance with Ch. 6, Para. D.4.c., Additional required documents:, in this Section.

vi) Advance Rate for Accounts Receivable Advance Rates:

(a) Eligible domestic accounts receivable: 85%.

(b) Eligible insured foreign accounts receivable: 90%

(c) Eligible accounts receivable for prime Federal contracts: 90%

(i) To be eligible as a prime Federal contract, the Lender must have obtained an assignment of the contract proceeds under the Assignment of Claims Act of 1940 (the Act), 31 U.S.C. 3727, or the Borrower is a subcontractor and the prime contractor has obtained an assignment under the Act, and the contract proceeds will be disbursed by a third-party funds control facility.

(d) The maximum advance rate cannot exceed 80% of the eligible receivables. The maximum advance rate may go up to 90% of the eligible receivables if the receivable is a prime Federal contract and the Lender has obtained an assignment of the contract proceeds under the Assignment of Claims Act of 1940 (the Act), 31 U.S.C. 3727, or the Borrower is a subcontractor and the prime contractor has obtained an assignment under the Act and the

contract proceeds will be disbursed by a third party funds control facility or the foreign accounts receivable are insured by the Export-Import Bank or a major private insurer. Additional exceptions may be permitted if the lender obtains SBA's prior written concurrence. The advance rate should not include any net profit. Factors that should be taken into consideration when determining the maximum advance rate are:

(i) Control and accounting systems of the Borrower;

(ii) Enhancements such as credit insurance;

(iii) Age of receivables;

(iv) Credit quality & Borrower's credit policy;

(v) Turnover history;

(vi) Industry orientation and condition; and

(vii) Net profit margin.

vii) Accounts Receivable Restrictions:

(a) The following types of accounts receivable are not eligible for inclusion in a Working Capital CAPLine:

(i) An account receivable that, by its original terms, is due and payable more than 180 calendar days from the date of the invoice, except those accounts receivable supported by acceptable letters of credit or credit insurance.

(ii) An account receivable that is subject to any adjustment, deduction, defense, dispute, or counterclaim, or the account receivable is contingent in any respect or for any reason.

(iii) Any portion of accounts receivable due from a credit-insured buyer that exceeds the limit established under the policy.

(iv) An account receivable due from an affiliated company.

(v) A foreign account receivable that is due and payable from a foreign buyer located in a country with which SBA is legally prohibited from doing business as identified in Note #7 in the EXIM Country Limitation Schedule.

(vi) An account receivable that the Lender deems uncollectible or unacceptable, including situations in which the items have been returned, rejected, or repossessed.

(vii) An account receivable that arises from a bill-and-hold, guarantee sale, sale-and-return, sale on approval, consignment,

or any other repurchase or return basis or is evidenced by chattel paper.

(viii) Offsetting account receivables and payables between the Borrower and one of its creditors (contra accounts). To determine net eligibility in these situations, the eligible accounts receivable must be reduced by the entire amount of the accounts payable.

(b) After initial disbursement, Lenders have unilateral authority to increase or decrease the advance rate for receivables by as much as 5% above or below the rate stated in the SBA Loan System. Increases or decreases in the advance rate above 5% require SBA's prior written concurrence.

viii) Inventory Advance Rate:

(a) The maximum advance rate cannot exceed 50% of eligible inventory. No advances are permitted on inventory located outside the United States.

(b) Exceptions are permitted if the lender obtains SBA's prior written concurrence. Factors to consider when determining the maximum advance rate are:

(i) Material and labor costs in manufacturing or invoice costs (less discounts) of resale goods in wholesale distribution;

(ii) Nature of the product;

(iii) Product liability;

(iv) Manufacturer's buyback agreements; and

(v) Physical location of inventory (single locations are generally easier to control than multiple locations).

ix) Inventory Restrictions:

(a) The following types of inventory are not eligible for inclusion in a Working Capital CAPLine.

(i) Inventory that is not subject to a valid, perfected, and enforceable first priority lien in favor of the Lender.

(ii) Inventory located at an address that has not been disclosed to the Lender in writing.

(iii) Inventory that is not located in the United States.

(iv) Inventory that is placed by the Borrower on consignment or held by the Borrower on consignment.

(v) Demonstration inventory.

(vi) Inventory that consists of proprietary software, spare parts, or any other class of inventory not intended for resale; and

(vii) Inventory that is damaged, obsolete, returned, defective, recalled, or unfit for further processing.

x) Annual and Renewal Credit Reviews

(a) On not less than an annual basis, and as part of any renewal of the loan, the Lender must obtain updated year end and interim financial statements and perform a full review of the credit and collateral securing the Working Capital CAPLine loan. The Lender's analysis must document that the Applicant:

(i) Is creditworthy.

(ii) Has the reasonable assurance of repayment in a timely manner from the conversion of sales into cash: and

(iii) Is in compliance with program requirements.

(b) If the Lender's analysis does not document that all three of the above requirements are met, no further disbursements may be made, and the loan may not be renewed until the Applicant can demonstrate that it meets the above three requirements.

(c) After initial disbursement, Lenders have unilateral authority to increase or decrease the advance rate for inventory by as much as 5% above or below the rate stated in the SBA Loan System. Increases or decreases in the advance rate above 5% require SBA's prior written concurrence.

xi) Examinations:

If the Working Capital CAPLine is over $1,000,000, Lender must conduct an annual field examination. The field examination may be conducted by the Lender's staff or a third party. An examination is a physical verification of the assets which compose the borrowing base. Examinations must include a sampling of the assets (receivables and inventory) included in the borrowing base. The frequency of the examinations may be determined by the Lender based upon the quality of the records, risk profile of the Borrower and seasonality of the line. At a minimum, an examination must be conducted prior to the initial disbursement and annually thereafter. The Lender must describe the level and frequency of examinations in the credit memorandum for the line.

xii) Loan Monitoring:

Most Working Capital CAPLines are administered using a Borrowing Base Certificate. When administering a line of credit with a BBC, below are the minimum requirements for the frequency of reporting. The Lender may require a BBC more frequently than stated below if it does so in accordance with the policies and procedures the Lender uses for its similarly-sized non-SBA guaranteed commercial lines. The minimum monitoring requirements for Working Capital CAPLines are as follows:

Monthly–- BBC; Aging of accounts receivable/payable; and Inventory listing (if advanced against);

Quarterly – Borrower prepared financial statements; and

(a) For Working Capital CAPLine loans of $2,000,000 or less, the Lender must obtain BBCs at least quarterly.

(b) For Working Capital CAPLine loans greater than $2,000,000, the Lender must obtain BBCs at least monthly.

xiii) BBC Collection

(a) The Lender must obtain the appropriate accounts receivable, accounts payable, and inventory reports necessary to determine its collateral position and for the coming period. Lenders may use their own forms for the BBC.

(b) Most Lenders require that the BBC be received by the 15th day of the following month. Lenders may choose when the BBC is due, but in no case may the due date be more than 30 calendar days after the end of a month.

(c) If the Borrower fails to submit the required monthly BBC to the Lender within 60 days of the month end, advances on the line of credit must stop until the BBC is obtained and the loan is confirmed to be In Margin.

(d) If the Borrower fails to submit the required quarterly BBC to the Lender within 30 days of the month-end, advances on the line of credit must stop until the BBC is obtained and the loan is confirmed to be In Margin.

(e) When the line is not in use with no outstanding principal balance and is not supporting the issuance of any letters of credit, the Lender may suspend the collection of Borrowing Base Certificates. Once suspended, the Lender must obtain a new BBC or complete a full credit memo documenting the current collateral position prior to making an advance.

(f) Annually – Borrowers management information system; legal elements; loan agreements; NAICS review; review of cash flow and related financials: and reassess exam, monitoring and control requirements.

(i) If the Working Capital CAPLine is $1,000,000 or less, credit review including cash flow analysis, concentration analysis, collateral analysis, owner/guarantor (except Supplemental Guarantors) credit review and annual site visit. Accounts from any one customer that constitute more than 20% of the total outstanding receivables should not be included in the eligible borrowing base unless the account is a public company with at least an A rating, a Federal government account, the customer has a long-standing positive credit history with the Borrower, the customer is a prime or sub-contractor performing on a Federal government contract, or the accounts are insured through credit insurance (common for foreign accounts receivable). If the account meets one of those five conditions, the Lender does not need to obtain SBA's prior written concurrence to include the account above the 20% in the eligible borrowing base but must include a written justification in the loan file. If, however, the account does not meet one of the five conditions, then the Lender must obtain SBA's prior written consent in order to include the account in the eligible borrowing base. Such requests must be sent to the LGPC.

xiv) If the Working Capital CAPLine is over $1,000,000, credit review including cash flow analysis, concentration analysis, collateral analysis, owner/guarantor (except Supplemental Guarantors) credit review and annual field examination. Accounts from any one customer that constitute more than 20% of the total outstanding receivables should not be included in the eligible borrowing base unless the account is a public company with at least an A rating, a Federal government account, the customer has a long-standing positive credit history with the Borrower, the customer is a prime or sub-contractor performing on a Federal government contract, or the accounts are insured through credit insurance (common for foreign accounts receivable). If the account meets one of those five conditions, the Lender does not need to obtain SBA's prior written concurrence to include the account above the 20% in the eligible borrowing base but must include a written justification in the loan file. If, however, the account does not meet one of the five conditions, then the Lender must obtain SBA's prior written consent in order to include the account in the eligible borrowing base. Such requests must be sent to the LGPC.

Loans that are not In Margin are Past Due.

If the Borrowing Base Certificate shows the Borrower is not In Margin or has not submitted a required BBC, the Lender must immediately require the Borrower to make a payment to reduce the loan balance to the point that it is within the borrowing base formula or obtain additional eligible collateral (i.e., marketable securities). The Lender must document their attempts to address the out-of-margin scenario in their credit file.

No additional advances may be made against a line that is not In Margin until the line is brought back in balance unless the Lender receives SBA's prior written consent through 7aLoanMod@sba.gov (regardless of whether the loan is processed on a non-delegated or PLP-WCP delegated basis).

ii. Level of Funds Control:

The level of funds control for a Working Capital CAPLine, whether a BBC is used or not, is determined by the banking relationship the lender has with the Borrower.

a) If the Lender has the Borrower's primary operating deposit accounts, the Lender is not required to use cash collateral accounts or other types of controlled accounts but must follow its established procedures for its similarly-sized, non-SBA guaranteed commercial lines of credit to monitor payments received.

b) If the Lender does not have the Borrower's primary operating deposit accounts, then the Lender must use some form of controlled account as follows:

i) The customers of the Borrower can be instructed to send their remittances via joint payee checks payable to lender and Borrower to the Lender; or

ii) Lock box (bank account under Lender control where Borrower's customers remit payments for accounts receivable).

3. Export Working Capital Program (EWCP) EWCP

a. Documentation specific to the EWCP financing request:

i. Copy of letter of credit and/or copy of buyer's order/contract, if applicable.

ii. Export credit insurance-related material (policy, application, buyer credit limit), if applicable.

iii. Copy of export license(s), if required.

iv. Aging of accounts receivable and accounts payable, and inventory reports

(dated within 180 days of application).

v. Cash flow projection statement with monthly (may be quarterly for asset-based loans) sales projections for the lesser of 12 months or the term of the loan, highlighting the proposed export transaction(s) to be financed. The cash flow may be limited to proposed export transaction(s) and/or based on anticipated export cash cycle, showing ability to complete projected export transaction(s) and repay the EWCP loan.

vi. If indirect exporting is being financed, a letter, invoice, order, contract, or other documentation from the Borrower's customer certifying that they will sell the goods/services purchased from the Borrower to a foreign buyer.

b. Copy of Lease, if applicable;

c. A detailed listing of all assets purchased with loan proceeds.

i. Non-Delegated EWCP:

a) Lender must submit applications via the SBA Loan System and notify the appropriate Export Finance Manager (as assigned to a USEAC) of the submission via email. A complete listing of Export Finance Manager locations and staff contact information is available.

b) The Export Finance Manager will conduct a full review and submit a recommendation to the LGPC. The LGPC will review the Export Finance Manager's recommendation, and the SBA Forms 1919 and Lender's application for guaranty for final approval.

c) If the LGPC declines the loan, the Lender may request reconsideration within 6 months of the date of decline by submitting a request to the LGPC. LGPC will forward the request for reconsideration for a final decision by the Director, International Trade Finance (D/ITF) or designee.

ii. PLP-EWCP applications – Lenders submitting applications using their delegated authority must submit guaranty applications via the SBA Loan System, retaining all required documentation in the Lender's loan file.

iii. See Chapter 6, SBA Terms and Conditions through Disbursement for all 7(a) Loans, for SBA requirements for post-approval and pre-disbursement requests for changes, transfer of guaranty between participating Lenders, and loan closing and disbursement.

**a. EWCP-Specific Post-Approval/Pre-Disbursement Requests for Changes**

i. For all EWCP loans, submit requests for changes to the appropriate Export Finance Manager unless the change is within the Lender's delegated PLP-EWCP authority.

ii. See Ch. 6, Para. B, Post-Approval Modifications, for additional guidance.

**b. EWCP-Specific Loan Closing and Disbursement Requirements**

See Ch. 6, Para. D of Section B for additional requirements for loan closing and disbursement.

i. Loan Terms: Under EWCP, there are two options for repayment. Advances on the line of credit must not occur unless the loan is In Margin. (See Loans that are not In Margin or are Past Due below):

a) Option 1: All cash and accounts receivable received are applied against the principal balance plus interest payments on outstanding balances;

i) Option 2: Interest-only payments on outstanding balances.

ii) EWCP with Master Notes, Sub-Notes, and Sub-Limits: EWCP loans may be structured with a Master Note to cover the total loan amount and general repayment period. Lenders can also use a system of sub-notes to establish specific repayment periods for specific purchase-orders, contract(s), or transactions. The conditions of the sub-notes must not conflict with the conditions of the Master Note, except for variances in repayment schedules. EWCP Asset Based Loans may be structured as a sublimit of a Master Note provided the sublimit conforms to the requirements of this Paragraph.

iii) See Ch. 6, Para. D.2 of Section B for additional requirements for Note terms.

ii. Advances and Receivables

a) On Single Transaction-Specific Loans and Transaction-Based Revolving Lines of Credit where draws are made against foreign purchase orders or contracts, the maximum advance rate is 90% of the purchase order/ contract or the Borrower's costs (including overhead), whichever is less. Foreign accounts receivable will be captured by the Lender through the use of a control account and applied against the outstanding loan balance.

b) On an asset-based revolving line of credit where advances are made against a borrowing base of foreign receivables and/or export-related inventory, the maximum advance rates are 90% on eligible foreign receivables and 75% on eligible export-related inventory located within the United States. Control accounts may be required at the discretion of the LGPC for non-delegated loans, or PLP-EWCP Lender for loans processed under delegated authority. At a minimum, the Borrower must submit a Borrowing Base Certificate (BBC) to the Lender at least monthly, or as frequently as the Lender customarily requires from its Borrowers on similarly-sized, non-SBA guaranteed loans if more often than monthly, along with an aging of foreign accounts receivable and

listing of export-related inventory, as appropriate. If the borrowing base shows the Borrower is over-advanced, the Lender must immediately require the Borrower to make a payment to reduce the loan balance so it is within the borrowing base formula.

c) Advance rates on foreign purchase orders/contracts or foreign accounts receivable when sold on open account (no credit insurance or letter of credit to mitigate the foreign risk) may not exceed 80%.

When approving uninsured buyers:

i) The exporter must provide favorable ledger experience with specific buyers over a significant period of time (at a minimum, 24 months) in countries with acceptable commercial or political risk. The limits extended on any uninsured buyers must be commensurate with the sales levels during the ledger history period; or

ii) The uninsured foreign accounts receivables are from credit-worthy buyers (e.g., financially sound corporations; multinational or publicly-traded companies), located in countries with acceptable commercial; or

iii) The uninsured foreign accounts receivables are from credit-worthy government entities in countries with acceptable commercial or political risk.

d) When establishing advance rates on uninsured foreign accounts receivable; the Lender must document its loan file with the analysis and justification to support the uninsured sale.

e) If the Lender is a PLP-EWCP Lender, the Lender may advance up to 90% against uninsured foreign accounts receivable when:

i) The uninsured foreign accounts receivables are from credit-worthy buyers (e.g., financially sound corporations; multinational or publicly-traded companies), located in countries with acceptable commercial; or

ii) The uninsured foreign accounts receivables are from credit-worthy government entities in countries with acceptable commercial or political risk.

When establishing an advance rate on uninsured foreign accounts receivable in excess of 80%, the PLP-EWCP Lender must document its loan file with the analysis and justification to support the higher advance rate.

f) Foreign Accounts Receivable:

i) Terms of Sale:

(a) Payment terms must be in compliance with the terms and conditions in the SBA Loan System. The Ex-Im Bank Country Limitation Schedule must be reviewed for prohibited countries (such countries are identified by Note # 7 on the Ex-Im Schedule) and the Department of Treasury OFAC sanctions lists must also be reviewed at sanctionssearch.ofac.treas.gov/.

(i) For federally-regulated Lenders, compliance with the procedures required by the Lender's Federal Financial Institution Regulator will constitute compliance with the above referenced OFAC requirement.

(ii) For SBA Supervised Lenders, Lender must check the OFAC sanctions lists prior to first disbursement of funds on each specific export transaction.

(b) Payment terms must be in line with prudent lending practices. Typical terms of sale include but are not limited to:

(i) Confirmed irrevocable letter(s) of credit (SBA or the PLP-EWCP Lender may require for some or all of the Borrower's foreign accounts). Foreign accounts receivable supported by acceptable letters of credit must not exceed 364 days from the invoice date;

(ii) Irrevocable letter(s) of credit (SBA or the PLP-EWCP Lender may require for some or all of the Borrower's foreign accounts). Foreign accounts receivable supported by acceptable letters of credit must not exceed 364 days from the invoice date;

(iii) Open account insured through Ex-Im Bank or private sector export credit insurance for comprehensive commercial and political risk (SBA or the PLP-EWCP Lender may determine that export credit insurance is required to enhance the quality of foreign accounts receivable. If export credit insurance is obtained, the Lender must be named as Loss Payee on the export credit insurance policy.) Foreign accounts receivable supported by credit insurance must not exceed 180 days from the invoice date;

(iv) Cash payment received prior to shipment;

(v) Open account uninsured, with SBA's prior written consent or documented by the PLP-EWCP Lender. Open account uninsured foreign accounts receivable must not exceed 180 days from the invoice date; and

(vi) Sight draft documents against payment, with SBA's prior written consent.

ii) Jurisdiction and Currency of Foreign Accounts Receivable: Foreign accounts receivable held as collateral should be payable to the Borrower in the United States and in United States dollars. Foreign accounts receivable due and payable in non-U.S. currency may be allowed on a case-by-case basis with SBA's prior written consent or authorized by the PLP-EWCP Lender. Depending on the stability of the currency in question, SBA may require that the Borrower mitigate the risk through hedging (purchasing of a forward currency contract, forward option, or similar mechanism) as a condition of such approval. When advancing against a transaction payable in a foreign currency, Lender must use an established foreign exchange rate and must retain documentation showing the exchange rate used and the Lender's calculation of the amount of the advance.

iii) Control Accounts:

(a) For the "single transaction-specific" and "transaction based-revolving line of credit" EWCP loans, Lenders will be required to set up a control account to capture the proceeds of foreign accounts receivable as they are paid by the foreign buyers. The proceeds are required to be applied against the loan balance, either in their entirety or as a percentage of the proceeds in a sufficient amount to pay off the initial advance for that specific transaction.

(b) For asset-based loans, LGPC for non-delegated loans, or the PLP-EWCP Lender for delegated loans, will determine if a control account is required based on the credit analysis. Normally, Lenders must have 100% of the foreign accounts receivable proceeds applied against the loan balance and have the Borrower request additional advances as needed based on a BBC. Another available option is to allow for the Borrower to maintain a balance within the Borrowing Base limits and to retain foreign accounts receivable proceeds (not applied to the loan balance upon collection). At a minimum, the Borrower must submit a BBC to the Lender at least monthly, or as frequently as the Lender customarily requires from its Borrowers on similarly-sized, non-SBA guaranteed loans if more than monthly, along with an aging of foreign accounts receivable and listing of export-related inventory, as appropriate. The Lender will review the Borrowing Base to ensure the Borrower is not over-advanced according to the available collateral detailed on the BBC. If the Borrower is over-advanced per the Borrowing Base, the Lender will require the Borrower to

immediately make a payment to reduce the loan balance to be in compliance. For a small business with an asset-based loan to be allowed to retain the foreign accounts receivable proceeds, the small business must:

(i) Be in business for at least 2 years (no start-ups); and

(ii) Have financial records satisfactory to SBA for non-delegated loans, or the PLP-EWCP Lender for delegated loans, and the ability to provide a current aging of foreign accounts receivable.

In deciding whether to permit a small business to retain the foreign accounts receivable proceeds, the PLP-EWCP Lender must comply with its policies and procedures for similarly-sized, non-SBA guaranteed credit facilities.

(c) Foreign Accounts Receivable Restrictions: Unless the Lender receives SBA's prior written consent, any of the following types of accounts receivable are not eligible for inclusion in an asset-based loan borrowing base:

(i) An account receivable that does not arise from the sale of items in the ordinary course of the Borrower's business;

(ii) An account receivable from a domestic (U.S.) company, unless the transaction has been approved by SBA as an indirect export;

(iii) An account receivable for which an invoice has not been sent;

(iv) An account receivable that is due and payable from a foreign buyer located in a country with which SBA is legally prohibited from doing business as set forth in the current Ex-Im Bank Country Limitation Schedule (such countries are identified by Note # 7 on the Schedule). (If the Borrower has knowledge that an export to a country in which SBA may do business, as set forth in the Ex-Im Bank Country Limitation Schedule, will be re-exported to a country with which SBA is legally prohibited from doing business, the corresponding receivables are not eligible for inclusion in the export-related borrowing base.);

(v) A foreign account receivable that, by its original terms, is due and payable more than 180 calendar days from the date of the invoice, except those accounts receivable supported by acceptable letters of credit or credit insurance;

(vi) A foreign account receivable that is still outstanding more than

60 calendar days from its original due date;

(vii) A foreign account receivable that the Lender deems uncollectible or unacceptable; this category includes, but not limited to, finance charges or late charges imposed on the foreign buyer by the Borrower as a result of the foreign buyer's past due status;

(viii) A foreign account receivable that does not comply with the terms of sale;

(ix) A foreign account receivable that arises from a bill-and-hold, guarantee sale, sale-and-return, sale on approval, consignment, or any other repurchase or return basis or is evidenced by chattel paper;

(x) A foreign account receivable that is subject to any offset, deduction, defense, dispute, or counterclaim, or the buyer is also a creditor or supplier of the Borrower or the account receivable is contingent in any respect or for any reason;

(xi) A foreign account receivable for which any of the items giving rise to such account receivable have been returned, rejected, or repossessed;

(xii) A foreign account receivable due from an affiliated company; and

(xiii) When 50% or more of the total foreign accounts receivable for a specific buyer are over 60 calendar days past the original due date, then the total foreign accounts receivable for that buyer are excluded.

(d) In addition, the Lender shall apply the same policies in reference to foreign accounts receivable eligible to be included in the borrowing base as the lender applies to its own similar asset-based loans which are not guaranteed by SBA or any other government entity.

(e) The Lender may verify that no ineligible foreign accounts receivable (as described above) are included in the borrowing base by obtaining a Borrower certification to this extent at the bottom of the BBC or on a separate certification form.

g) Export-Related Inventory:

i) General Guidelines:

(a) Export-related inventory taken as collateral must be located within the United States, until shipped to the foreign buyer.

(b) Export-related inventory must be valued at the lower of actual cost or market value (including cost of work-in-process inventory) as determined in accordance with Generally Accepted Accounting Principles (GAAP).

(c) Export-related inventory may include raw materials, work-in-process, and finished goods.

(d) Advance rates against eligible export-related inventory may vary depending on inventory quality.

ii) Export-Related Inventory Restrictions: Unless the Lender receives SBA's prior written consent, any of the following types of export-related inventory are not eligible for inclusion in the export-related borrowing base:

(a) Export-related inventory that is not subject to a valid, perfected, and enforceable first priority lien in favor of the Lender;

(b) Export-related inventory located at an address that has not been disclosed to the Lender in writing;

(c) Export-related inventory that is not located in the United States;

(d) Export-related inventory that is placed by the Borrower on consignment or held by the Borrower on consignment;

(e) Export-related inventory that is demonstration inventory;

(f) Export-related inventory that consists of proprietary software (i.e., software designed solely for the Borrower's internal use and not intended for resale);

(g) Export-related inventory that is damaged, obsolete, returned, defective, recalled, or unfit for further processing; and

(h) Export-related inventory that is to be incorporated into items destined for shipment to a country with which SBA is legally prohibited from doing business as designated in the current Ex-Im Bank Country Limitation Schedule (such countries are identified by Note # 7 on the Schedule), or that the Borrower has knowledge will be re-exported by a foreign buyer to a country in which SBA is legally prohibited from doing business.

iii) In addition, Lender shall apply the same policies in reference to export-related inventory eligible to be included in the borrowing base as the Lender applies to its own similarly-sized, asset-based loans which are not guaranteed by SBA or any other government entity.

iv) The Lender may verify that no ineligible export-related inventory (as described above) is included in the borrowing base by obtaining a

Borrower certification to this extent at the bottom of the BBC or on a separate certification form.

h) Field Examinations.

i) The Lender must perform a field examination prior to the first disbursement on all Asset-Based EWCP loans that are $1,000,000 or greater.

ii) Lenders are not required to perform field examinations on Transaction-Based EWCP loans, as each transaction is reviewed individually by the institution.

iii) The field examination is an out-of-pocket expense and may be conducted by the Lender's internal audit staff or a third-party examiner. An examination is a verification of the assets that compose the borrowing base. Examinations must include a sampling of the assets (receivables and inventory) included in the borrowing base.

iv) If the Asset-Based EWCP loan is $2,000,000 or greater, the Lender must conduct a field examination at least annually.

v) For Asset-Based EWCP loans less than $2,000,000: After the initial field exam prior to the first disbursement (if applicable), the frequency of field examinations may be determined by the Lender based upon the quality of the records, risk profile of the Borrower and seasonality of the line. If the Lender determines that a field examination is not necessary as part of the annual review, the Lender must document the specific circumstances that enabled the decision. Acceptable criteria for not conducting an annual field examination for loans of less than $2,000,000 includes but is not limited to: overall line utilization, level of inventory reliance, suppressed availability, etc.

i) Borrowing Base Certificates.

i) All Asset-Based RWCP loans must be administered using a Borrowing Base Certificate. The Lender may require a BBC more frequently than stated below if it does so in accordance with the policies and procedures the Lender uses for its similarly-sized non-SBA guaranteed commercial lines.

ii) For EWCP loans of $1,000,000 or less, the Lender must obtain BBCs at least quarterly.

iii) For EWCP loans greater than $1,000,000, the Lender must obtain BBCs at least monthly.

iv) A Lender may require BBC submissions with each draw on the line to support a line structure that updates the accounts receivable

availability throughout the month. To administer this method, the Lender must obtain a new BBC with each draw. BBCs used to support a draw that occurs before a monthly BBC is due must identify the new billings and collections that occurred since the last certificate was received.

j) BBC Collection.

i) The Lender must obtain the appropriate accounts receivable, accounts payable, and inventory reports necessary to determine their collateral position and for the coming period. Lenders may use their own forms for the BBC.

ii) Most Lenders require that the BBC is received by the 15th day of the following month. Lenders may choose when the BBC is due, but in no case may the due date be more than 30 calendar days after the end of a month.

iii) If the Borrower fails to submit the required monthly BBC to the Lender within 60 days of the month end, advances on the line of credit must stop until the BBC is obtained and the loan is confirmed to be In Margin.

iv) If the Borrower fails to submit the required quarterly BBC to the Lender within 30 days of the month end, advances on the line of credit must stop until the BBC is obtained and the loan is confirmed to be In Margin.

v) When the line is not in use with no outstanding principal balance and is not supporting the issuance of any letters of credit, the Lender may suspend the collection of Borrowing Base Certificates. Once suspended, the Lender must obtain a new BBC or complete a full credit memo documenting the current collateral position prior to making an advance.

k) Loans that are not In Margin or are Past Due.

i) If the Borrowing Base Certificate shows the Borrower is not In Margin or has not submitted a required BBC, the Lender must immediately require the Borrower to make a payment to reduce the loan balance to the point that it is within the borrowing base formula or obtain additional eligible collateral (i.e. marketable securities). The Lender must document their attempts to address the out-of-margin scenario in their credit file.

ii) No additional advances may be made against a line that is not In Margin until the line is brought back in balance unless the Lender receives SBA's prior written consent through 7aLoanMod@sba.gov

(regardless of whether the loan is processed on a non-delegated or PLP-EWCP delegated basis).

l) Certifications:

i) The Borrower must certify that appropriate withholding tax deposits on advances for payroll have been made and that no loan proceeds will be used to pay delinquent withholding taxes or other similar trust funds (state sales tax, etc.). The Lender may include this certification as part of its Borrowing Base Certification reporting package.

ii) The Borrower must provide a copy of valid export license(s) for each different product, and each different country, or a letter from the Borrower stating a valid export license(s) is not required, citing the authority for this statement. The Borrower may provide these items with a Borrowing Base Certification reporting package.

4. International Trade (IT) Loans:

a. Reconsideration of declined non-delegated IT applications (13 CFR § 120.193):

i. If the Lender believes the reason(s) for decline have been overcome, a request for reconsideration may be submitted along with a detailed written explanation of how the Applicant has overcome the reason(s) for decline. Lender must submit a request for reconsideration to the LGPC within 6 months of the date of decline. Any request submitted more than 120 days after the date of decline must include current financial statements.

ii. If a request for reconsideration is declined by the LGPC, a second reconsideration may be requested from the D/FA or designee, whose decision is final. The request to the D/FA or designee must be submitted to the LGPC and must include a copy of the Center's decline letter and include additional information that specifically addresses the reason(s) identified for decline and how the Applicant has overcome those reason(s). The LGPC will forward the request to the D/FA or designee for a final decision.