

## SOP 50 10(5) Frequently Asked Questions

### Eligibility – Passive Income

1. **Q:** When the applicant is a mini-warehouse or other type of business that receives passive income, how does the lender document that at least 50% of the revenue is derived from services provided?

**A:** The applicant must break down the revenue into the passive income (rental) and income for services provided. If the applicant is unable to break down the revenue and show that at least 50 % of its revenue is derived from services provided, then the applicant is not eligible.

2. **Q:** When the applicant is a mini-warehouse or other type of business that is a start-up, how does the lender document that at least 50% of the revenue is derived from services provided?

**A:** The applicant's projections must break down the revenue into the passive income (rental) and the income for services to be provided in order to make a determination that the applicant is eligible.

3. **Q:** When the applicant does not bill separately for services and has the majority of its revenue as passive income (rental), how does a lender determine if it is eligible?

**A:** If expenses associated with providing the services equal at least 50 % of the total revenue earned by the applicant, then the applicant is eligible. SBA does not consider mortgage payments, depreciation, etc. as "expenses associated with providing services."

### Eligibility – Limited or Special Use Property

1. **Q:** Swimming pools are listed as a Limited or Special Purpose Property. If the applicant has a pool on the property is it a Limited or Special Purpose Property?

**A:** If the applicant has a pool on the property and is in the business of providing recreation through the use of a swimming pool, then it is a Limited or Special use Property.

2. **Q:** Does SBA consider all day care centers to be Limited or Special Purpose Properties?

**A:** SBA does not consider day care centers to be Limited or Special Purpose Properties. If, however, the facility is a pre-school as well as a day care center, then it would be a Limited or Special Purpose Property. It depends on the specific circumstances surrounding that particular business.

### Eligibility – Trade with Foreign Countries

1. **Q:** How does a Lender or CDC determine if an applicant involved in international trade is doing business with a country where the U.S. Government has implemented trade restrictions which would cause the applicant to be ineligible for SBA assistance?

A: The Lender or CDC must review the Export-Import Bank’s Country Limitation Schedule as explained in the SOP. If the applicant does business with a country that is identified with Note #7, then the applicant is not eligible for 7(a) or 504 assistance. If the country is identified with any other code, the applicant is eligible and the application can be processed under any of SBA's delivery methods.

#### Eligibility – 504 – Machinery and Equipment

1. Q: Are locomotives, dumpsters, and forklifts eligible for 504 financing?

A: Locomotives are not eligible. In the case of dumpsters and forklifts, if the business should have one or two associated with the purchase of a building it would be eligible. It would not be eligible if the request was for someone who is in the business of supplying dumpsters or forklifts as it is not equipment in a fixed location or meet the definition of heavy duty construction equipment.

#### Change of Ownership

1. Q: In a change of ownership, if the Lender does not know if the seller has SBA-guaranteed financing, can the loan be processed using PLP procedures?

A: After the lender has documented its efforts to determine if the seller has SBA-guaranteed financing, the application can be processed PLP if the seller does not have SBA-guaranteed financing or the lender was unable to determine if the seller has SBA-guaranteed financing.

2. Q: In a change of ownership, the SOP mentions the lender should explore seller financing for intangibles. If the seller is unwilling to finance all or a portion of the intangibles, what is the Lender’s documentation responsibility?

A: The lender should document its efforts to obtain seller financing. The documentation should include a copy of a letter or email to the seller along with a copy of the seller’s response or a specific notation that a response was not received within 15 business days. In addition, attempts at telephonic communication should also be documented.

3. Q: In the 504 program, is a “change of ownership” considered a “new business?”

A: Yes, SBA considers a change of ownership to be a “new” business because it will result in new, unproven ownership/management and increased debt unrelated to business operations.

#### Personal Guaranties

1. Q: If a borrower is going to use a 401(k) to own all or a portion of a business, is the 401(k) required to guarantee all or a portion of the loan?

A: No. Under the provisions of the new SOP, the 401(k) does not have to guarantee the loan; however, the Employee Participant (owner(s) of the Qualified Retirement Account, the new 401(k)

that owns a portion of the business) must provide a full, unconditional personal guaranty. In addition, the Lender or CDC must ensure that the 401(k) plan meets the applicable IRS eligibility requirements.

### Refinancing

1. Q: If the loan will be refinancing a business acquisition, what is the maximum maturity?

A: The maturity of the SBA-guaranteed loan will be based on the remaining useful life of the business collateral being pledged to secure the loan.

2. Q: Is interest-only financing considered unreasonable and, therefore, eligible to be refinanced with an SBA-guaranteed loan?

A: Interest-only term debts are considered unreasonable. A short term, interest only line of credit is not considered unreasonable because this is a standard means of financing short term working capital needs.

3. Q: Does the 20% cash flow improvement rule apply to short term lines of credit?

A: No.

4. Q: Do all of the tests associated with debt refinancing for SBA Express apply to Patriot Express and the Pilot Loan Programs?

A: Yes. Questions regarding debt refinancing are on the Eligibility Checklist covering all these programs.

### 912 Issues

1. Q: If a borrower had prior offenses and the application previously was cleared for processing by SBA, will this applicant have to be cleared for those offenses again?

A: Yes, the applicant must complete a new 912 in connection with the new application. The 912 must go through the appropriate clearance process.

2. Q: If the applicant has a criminal record which has been expunged, how should the applicant answer the questions on SBA Form 912?

A: Although the record may have been expunged, in many cases the arrest record still exists so the applicant must answer "yes" to the question asking if he/she has ever been arrested. The applicant can explain that the record related to the arrest has been expunged. The lender will need to submit the completed 912 package for the required name check/character determination.

3. Q: If there is no paperwork to show the charges were dropped without prosecution, what can the borrower/Lender/CDC do?

A: If there is no paperwork from the court or prosecutor's office to support the claim that the charge was dropped without prosecution, the complete 912 package must be submitted for a name check/character determination.

### INS/USCIS Verification

1. Q: When making a second loan to a borrower that received a loan, is a new verification of alien status required?

A: If the verification is for a Lawful Permanent Resident, verification is required if 6 months has elapsed since the last verification with one exception: If the individual reported an offense on SBA Form 912, then verification would be required even if 6 months had not elapsed, as the offense may put their status at risk. For non-Lawful Permanent Residents, verification is required with each request, as their status can be revoked at any time.

### Collateral

1. Q: Under 7(a), does a Lender have to take all available collateral, even if the value may be considered negligible?

A: For 7(a) loans other than SBA Express and the Pilot Loan Programs, the Lender must take security interests in all available assets with a combined "liquidation value" up to the loan amount. For SBA Express and the Pilot Loan Programs, the Lender uses the same collateral policies it has for its non-SBA loans with one exception: For Patriot Express loans of \$350,000 or more, the Lender must take all available collateral.

### Appraisals

1. Q: When the collateral will be new construction or involve substantial renovation of an existing building, can a Certificate of Occupancy or Lender/CDC's site visit meet the requirement for a post-construction certification by an appraiser?

A: No, the appraiser will know the rationale for the "as-built" value of the structure and is the person in the best position to determine if the value of the structure needs to be adjusted as a result of any deviations from the original plans and specifications.

2. Q: When the collateral will be new construction or involve substantial renovation of an existing building, the appraisal must estimate what the market value will be at completion of construction. After construction is completed, the lender must obtain a certification from the appraiser that construction was completed according to plans and specifications. What is SBA requiring the appraiser to certify to?

A: SBA is requiring that the appraiser review the project after construction has been completed to determine whether the finished project still meets the original appraised value or if the appraisal needs to be adjusted to reflect substantial changes in the final project from the original plans and

specifications. Changes in market conditions that may have occurred during the construction period are not to be reflected in the final determination of appraised value.

3. **Q:** If the valuation of fixed assets is greater than their depreciated value, an independent appraisal must be obtained to support the higher valuation according to the SOP. Does this apply to SBA Express?

**A:** No. The SOP describes the SBA Express collateral policy separately and should be read to include the Lender's appraisal policy.

4. **Q:** In 7(a), SBA requires a real estate appraisal if the SBA-guaranteed loan is greater than \$250,000 and is secured by commercial real property. Would an appraisal be required in the situation where the lender has taken an "abundance of caution" lien on real estate and given no value to it?

**A:** Yes, if it is commercial property. The Small Business Act requires an appraisal on any commercial real property that secures a 7(a) loan that is over \$250,000.

5. **Q:** For 504, when land for the project property is contributed as all or part of the borrower's contribution, when is an appraisal required?

**A:** It is required at the time of application to determine if the required borrower's contribution has been satisfied. If it has not been satisfied, additional cash or land (which will be part of the project property) must be injected. The borrower's contribution must be satisfied for the 504 application to be eligible.

### Business Valuation

1. **Q:** Can Lenders use third party software to constitute an independent business valuation?

**A:** No, because the lender inputs the data into the software program it is not an independent, third party valuation.

### Financial Statement/Documentation Requirements

1. **Q:** What does SBA mean when it uses the phrase "date of application," in connection with the requirement for an applicant's financial statements to be no older than 90 days from the date of application?

**A:** In this instance, when SBA uses the phrase "date of application," it means the date the application was received by SBA (not the lender). Thus, an applicant's financial statements must be no older than 90 days from the date that SBA receives the application.

2. **Q:** What documentation must the lender have in its file to satisfy SBA requirements concerning the verification of an applicant's tax returns when the IRS transcript reflects "Record Not Found" for one of the three years requested? For example, the lender requests transcripts for 2002, 2003 and 2004 and the 2003 transcript shows "Record Not Found."

A: If the IRS has record of the returns filed in the previous and subsequent years, the Lender has verified these tax returns, AND the borrower has some record of either receiving a refund or paying the taxes for the missing year, then the Lender may reasonably assume that the borrower filed a return for the missing year. Additionally, having the borrower take a copy of the missing return to the local IRS office and having the office acknowledge receiving it is further evidence that the IRS has received the return. If the Lender documents all of these steps in its loan file, the lender would be able to show to SBA that it made good faith efforts to satisfy the verification requirement.

### Maximum Maturity

1. Q: What does SBA consider as the maximum term for financing intangibles?

A: 10 years.

### Insurance

1. Q: The SOP requires Lenders and CDCs to include in the Authorization any other insurance appropriate to the loan and includes a list of other types of insurance. Are the insurance types listed required?

A: The Lender/CDC has the discretion to determine what other insurance should be required.

### PLP Processing

1. Q: Can applications involving medical facilities or farms be processed under PLP procedures?

A: Yes, the prohibitions against PLP processing for certain types of businesses have been removed.

2. Q: Has the requirement for a 10% equity injection for new businesses, change of ownerships or the purchase of real estate been removed as a requirement for such applications to be processed under PLP?

A: Yes.

### Disbursement

1. Q: Does the 48-month disbursement period limit apply to all 7(a) and 504 loan programs, including SBA Express and the Pilot Loan Programs?

A: Yes. If you reach the 48 month period and the loan is not fully disbursed, the loan must be disbursed or any remaining balance canceled. If the loan is not disbursed at all, a new application can be processed with updated financial information. With revolving lines of credit, SBA views the loan as being fully disbursed with the initial disbursement.

2. Q: After the borrower signs the SBA Form 1050 at initial disbursement, is the Lender required to continue to list all subsequent disbursements on the Form 1050?

A: No. Each disbursement must be documented, but there is no need to go back and add all the disbursements onto the Form 1050. The form is only required at time of first disbursement.

#### Lender Fees

1. Q: Can a lender charge a borrower a prepayment penalty?

A: No, Agency regulations at 13 CFR 120.221(e) specifically prohibit lenders from charging prepayment penalties on SBA-guaranteed loans.

#### Program Guides

1. Q: Will the program guides be updated?

A: No, when SBA updates SOP 50 50 and SOP 50 51, the appropriate sections from the program guides will be incorporated into each SOP and then the program guides will be eliminated.

#### CDC Organization Requirements

1. Q: If a CDC has in its by-laws that less than 51% of the membership constitutes a quorum, does the CDC have to change its by-laws?

A: Yes, the by-laws should be changed at the earliest opportunity and must be changed prior to the next CDC status renewal or review.