SBA Information Notice

TO: All SBA Employees, 7(a) Lenders, Certified Development Companies, Microloan Intermediaries, and Intermediary Lending Pilot Program Intermediaries

CONTROL NO.: 5000-20003

EFFECTIVE: March 11, 2020

SUBJECT: Publication of Interim Final Rule – Express Loan Programs; Affiliation Standards

The purpose of this Notice is to announce the publication of the Interim Final Rule on Express Loan Programs; Affiliation Standards in the Federal Register on February 10, 2020, at https://www.govinfo.gov/app/details/FR-2020-02-10/2020-02128.

SBA is amending various regulations governing its business loan programs, including the SBA Express and Export Express Loan Programs and the Microloan and Development Company (504) loan programs. SBA previously published a Notice of Proposed Rulemaking addressing all of the topics and issues covered by this interim final rule. (83 FR 49001, September 28, 2018) In order to provide the public with an additional opportunity to comment, SBA published this as an interim final rule rather than proceeding to a final rule. The rule will become effective March 11, 2020; however, as detailed below, compliance with two of the regulatory changes will not be required until October 1, 2020. All stakeholders are encouraged to read the interim final rule thoroughly. SOP 50 10 will be updated to reflect these changes.

The interim final rule addresses the following topics:

1. SBA Express and Export Express Loan Programs (13 CFR §§ 120.441 -120.447**)**

SBA has codified into regulation the existing requirements unique to the SBA Express and Export Express loan programs. Additionally, all other parts of this rule that apply to the 7(a) loan program, including the provisions relating to the fees a Lender may charge an Applicant or Borrower, also apply to the SBA Express and Export Express programs.

2. Size standards and Affiliation Principles (13 CFR § 121.301(f)(4)-(7))

a. *Identity of Interest*: SBA revised the factors it will consider when determining whether affiliation exists based on identity of interest to include:

Close relatives: Affiliation arises where there is an identity of interest between close relatives, as defined in 13 CFR § 120.10, with identical or substantially identical economic interests.

Common investments: Affiliation arises through common investments where the same individuals or firms together own a substantial portion of multiple concerns in the same or related industry, and such concerns conduct business with each other, or share resources, equipment, locations, or employees with one another, or provide loan guaranties or other financial or managerial support to each other.

However, where an SBA Lender has made a determination of no affiliation under this ground, SBA will not overturn that determination as long as it was reasonable when made given the information available to the SBA Lender at the time.

Economic dependence: Affiliation based upon economic dependence may arise when a concern derived more than 85 percent of its receipts over the previous three fiscal years from a contractual relationship with another concern, except that no affiliation will be found if:

Exception 1: The contract (or contracts) does not restrict the concern in question from selling the same type of products or services to another purchaser;

Exception 2: SBA reviews the contract and agrees that the terms of the contract (or contracts) do not provide the purchaser of goods or services with control or the power to control the seller (the Applicant small business).

Note for Exception 2: SBA has made available guidance on the process for requesting SBA review of a contract and the factors SBA will consider in determining whether there is control under Exception 2. The guidance can be found at https://www.sba.gov/offices/headquarters/oca/spotlight. SBA is accepting comments on this guidance through April 10, 2020, at affiliation.comments@sba.gov.

b. Newly organized concern: Affiliation may arise where current or former officers, directors, owners of a 20 percent interest or greater, managing members, or persons hired to manage day-to-day operations of one concern organize a new concern in the same or related industry or field of operation, and serve as the new concern's officers, directors, owners of a 20 percent interest or greater, or managing members, and there are direct monetary benefits flowing from the new concern to the original concern. A concern may rebut such an affiliation determination by demonstrating a clear line of fracture between the two concerns. A concern will be considered "new" for the purpose of this paragraph if it has been actively operating for two years or less.

However, where an SBA Lender has made a determination of no affiliation under this ground, SBA will not overturn that determination as long as it was reasonable when made given the information available to the SBA Lender at the time.

c. Affiliation based on totality of the circumstances: In determining whether affiliation exists, SBA may consider all connections between the concern and a possible affiliate. Even though no single factor is sufficient to constitute affiliation, SBA may find affiliation on a case-by-case basis where there is clear and convincing evidence based on the totality of the circumstances.

However, where an SBA Lender has made a determination of no affiliation, SBA will not overturn that determination as long as it was reasonable when made given the information available to the SBA Lender at the time.

d. Affiliation based on franchise agreements: SBA clarified that the term ''franchise'' means any continuing commercial relationship or arrangement, whatever it may be called, that meets the the Federal Trade Commission's definition of ''franchise'' in 16 CFR part 436. SBA also added to this regulation a statement that SBA will maintain a publicly available centralized lists of franchise and other similar agreements that are eligible for SBA financial assistance, consistent with SBA's current policy and procedure.

3. Personal Resources Test - Funds not available from alternative sources, including the personal resources of owners (13 CFR § 120.102)

SBA has reinstituted a personal resources test to aid SBA Lenders in determining whether an Applicant has access to credit elsewhere, including from the personal resources of the owners.

An Applicant for a business loan must show that the desired funds are not available from the resources of any individual or entity owning 20 percent or more of the Applicant. SBA will require the use of liquid assets from any such owner as an injection to reduce the SBA loan amount when that owner's liquid assets exceed certain amounts. These funds must be injected prior to the disbursement of the proceeds of any SBA financing. The amount to be injected is determined based on the "total financing package." The total financing package includes the SBA loan, together with any other loans, equity injection, or business funds used or arranged for at or about the same time (i.e., within 90 days) for the same project as the SBA loan.

When the total financing package is:

- $350,000 or less, each 20 percent owner of the Applicant must inject any liquid assets that are in excess of two times the total financing package, or $500,000, whichever is greater;
- Between $350,001 and $1,000,000, each 20 percent owner of the Applicant must inject any liquid assets that are in excess of one and one-half times the total financing package, or $1,000,000, whichever is greater; or
- Greater than $1,000,000, each 20 percent owner of the Applicant must inject any liquid assets that are in excess of one times the total financing package, or $2,500,000, whichever is greater.

The regulation contains the definition of "liquid assets" and SBA will provide additional examples in the updated SOP 50 10.

4. 7(a) Lender Fees - Fees and expenses that the Lender may collect from an Applicant or Borrower (13 CFR § 120.221(a))

SBA revised 13 CFR § 120.221(a) to simplify the fees a 7(a) Lender may collect from an Applicant for assistance in obtaining an SBA-guaranteed loan.

Through September 30, 2020, 7(a) Lenders may choose on a per-loan basis either Option A or Option B below. Beginning October 1, 2020, 7(a) Lenders must use Option B below.

Regardless of which option the 7(a) Lender uses, it must complete an SBA Form 159, Fee Disclosure and Compensation Agreement.

Option A. **(Available Through September 30, 2020) -** A 7(a) Lender may charge an applicant reasonable fees (customary for similar Lenders in the geographic area where the loan is being made) for packaging services. "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 fees a 7(a) Lender may charge an Applicant for packaging services:

i. Must be reasonable and customary for the services actually performed;

ii. Must be consistent with those fees the 7(a) Lender charges on its similarly-sized, non-SBA guaranteed commercial loans; and

iii. May be 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.

a) For fees charged 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.

b) For fees charged based on a percentage of the loan amount, the fee may not exceed:

i) 3% on loans of $50,000 or less;

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

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

Option B. **(Mandatory Beginning October 1, 2020 and Optional through September 30, 2020)** - Regardless of what the fee is called (e.g., origination fee, application fee, etc.), a 7(a) Lender will be permitted to collect a fee from the Applicant for assistance in obtaining an SBA-guaranteed loan.

i. The fee may not exceed $3,000 for a loan up to and including $350,000 and no more than $5,000 for a loan over $350,000.

ii. The 7(a) Lender must advise the Applicant in writing that the Applicant is not required to obtain or pay for unwanted services.

iii. In cases where the 7(a) Lender charges any fee to the Applicant in excess of those specified above, the Lender must reduce the charge and refund to the Applicant any amount in excess of the permitted fee.

iv. If the 7(a) Lender charges the Applicant a fee for assistance in obtaining an SBA-guaranteed loan, the 7(a) Lender must disclose the fee on SBA Form 159, under "Type of Services, Other," as "Lender Fee." The 7(a) Lender is not required to itemize the fees charged to the Applicant.

5. 7(a) Lender Extraordinary Servicing Fees - Fees and expenses that the Lender may collect from an Applicant or Borrower (13 CFR §§ 120.221(b) and 120.344(b))

SBA revised 13 CFR § 120.221(b) to permit extraordinary servicing fees in excess of 2 percent per year for Export Working Capital Program (EWCP) loans and Working Capital CAPLines that are disbursed based on a Borrowing Base Certificate. In these programs, the fees charged will need to be reasonable and prudent based on the level of extraordinary effort required and cannot be higher than the fees charged on the Lender's similarly-sized, non-SBA guaranteed commercial loans.

SBA made a conforming amendment to 13 CFR § 120.344(b) to ensure that the extraordinary servicing fees charged on EWCP loans, as permitted by the revised 13 CFR § 120.221(b), are reasonable and prudent.

6. Key Definitions (13 CFR § 103.1)

SBA revised the definitions of the categories of Agents, including Lender Service Provider (LSP), Packager, and Referral Agent and moved them into 13 CFR § 103.1(a) (the definition of "Agent").

The definition of Agent is revised 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. For purposes of SBA's business loan programs, the term Agent includes but is not limited to:

a. Lender Service Provider: An Agent who assists the Lender with originating, disbursing, servicing, liquidating, or litigating SBA loans. The Lender bears full responsibility for all aspects of its SBA loan operation, including, but not limited to, approvals, closings, disbursements, servicing actions, and due diligence. Lender Service Providers may only receive compensation from the Lender and such compensation may not be passed on to the Applicant or paid out of SBA-guaranteed loan proceeds.

b. Packager: An Agent who prepares the Applicant's application for financial assistance and is employed and compensated by the Applicant.

c. Loan Broker (also known as Referral Agent): An Agent who, on a specific transaction, either assists the Applicant in finding an SBA Lender that will be willing to make a loan

to the Applicant or assists the SBA Lender in finding an Applicant. A Loan Broker may be employed and compensated by either the Applicant or the SBA Lender (but not both). Compensation paid to a Loan Broker by an SBA Lender may not be passed on to the Applicant and may not be paid out of SBA-guaranteed loan or debenture proceeds.

Based on these revised definitions, some Agents may need to enter into LSP agreements with the Lenders to which they provide services. If an LSP Agreement is required, the agreement must be submitted to SBA for review in accordance with 13 CFR § 103.5. SBA will permit Agents and Lenders a period of 120 days from the date of publication of the interim final rule (until June 9, 2020) in order to enter into an LSP agreement that has been reviewed by SBA. SBA will work with Agents and Lenders to help them meet that deadline.

7. Two master prohibition - What is "good cause for suspension or revocation? (13 CFR § 103.4)

SBA eliminated the limited exception to the two-master prohibition currently contained in 13 CFR § 103.4(g). Effective March 11, 2020, regardless of the service(s) provided, SBA no longer permits an Agent, including an LSP, to provide services to both the Applicant and the SBA Lender and be compensated by both parties in connection with the same loan application.

For purposes of this paragraph, the actions of an Agent include the actions of the Agent's Affiliates (as defined in 13 CFR § 121.103). Therefore, an Agent cannot use a separate (but related) entity to circumvent the two-master prohibition.

If an Agent, including an LSP, provides services to both the Applicant and the SBA Lender and is compensated by both parties in connection with the same loan application prior to March 11, 2020, it is very important that the dates of the services provided be documented in the loan file.

8. Fees an Agent may charge an Applicant – How does SBA regulate an Agent's fees and provision of service? (13 CFR § 103.5(b) and (c))

a. *Total Agent fees charged to Applicant.* SBA revised 13 CFR § 103.5(b) to reflect the amounts SBA has determined to be reasonable for the total compensation that an Applicant can be charged by one or more Agents for assistance in obtaining a 7(a) or 504 loan.

Through September 30, 2020, Agents may use either Option A or Option B below. Beginning October 1, 2020, Agents must use Option B below.

Regardless of which option the Agent uses, it must complete an SBA Form 159 and provide supporting documentation as required by Loan Program Requirements (as defined in 13 CFR § 120.10).

***Option A*. (Available Through September 30, 2020) -** 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 following stated maximums):

- 3 percent on loans of $50,000 or less;
- 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,
- The maximum fee that may be charged in the aggregate to an Applicant on a percentage basis is $30,000.

Option B. **(Mandatory Beginning October 1, 2020 and Optional through September 30, 2020)** - Total compensation charged by an Agent or Agents to an Applicant for services rendered in connection with obtaining a 7(a) or 504 loan must be reasonable.

i. SBA considers the following amounts to be reasonable for the total compensation that an Applicant can be charged by one or more Agents:

- For loans up to and including $500,000: a maximum of 3.5% of the loan amount, or $10,000, whichever is less;
- For loans $500,001-$1,000,000: a maximum of 2% of the loan amount or $15,000, whichever is less; and
- For loans over $1,000,000: a maximum of 1.5% of the loan amount, or $30,000, whichever is less.

ii. These maximum limits apply regardless of whether the Agent's fee is based on a percentage of the loan amount or on an hourly basis. (These maximums do not apply if the fee is being paid by the SBA Lender.)

If an Agent provides more than one service to an Applicant (e.g., packaging and referral services), only one fee is permitted for all services performed by the Agent.

If more than one Agent (e.g., a Packager and a Loan Broker/Referral Agent) provides assistance to the Applicant in obtaining the loan, the total amount of all fees that the Applicant is required to pay must not exceed the maximum allowable fee described above. (However, a fee charged to the Applicant by the Lender in accordance with 13 CFR § 120.221(a) or by the CDC in accordance with 13 CFR § 120.971(a) will not be counted toward the maximum allowable fee for an Agent or Agents.)

If an Agent or Agents charge an Applicant fees in connection with obtaining an SBA-guaranteed loan, the Agent(s) must disclose the fees to SBA by completing SBA Form 159 and providing supporting documentation as required by Loan Program Requirements.

b. *Agent fees paid by SBA Lender.* Effective March 11, 2020, SBA modified 13 CFR § 103.5(c) to clarify that any fees the SBA Lender pays to an Agent for services in connection with a 7(a) or 504 loan may not be passed on to the Applicant either directly or indirectly.

9. Definition of Associate of a Lender or CDC (13 CFR § 120.10)

The definition of an Associate of a Lender or CDC has historically included, among others, "an agent involved in the loan process." In order to provide more clarity for SBA Lenders and their Associates, SBA modified this definition to capitalize the term "Agent" and add a parenthetical to clarify that "an Agent involved in the loan process" means an Agent, as that term is defined in 13 CFR 103.1.

10. Loans to Qualified Employee Trusts (13 CFR §§ 120.350 and 120.352)

SBA made a technical amendment to both 13 CFR § 120.350, Policy, and 13 CFR § 120.352, Use of Proceeds, to incorporate the recent statutory change that permits SBA to guarantee a loan to the small business concern (rather than the qualified employee trust), if the proceeds from the loan are used only to make a loan to a qualified employee trust that results in the qualified employee trust owning at least 51 percent of the small business concern.

11. Lender's Responsibility When Purchasing 7(a) Loans from the FDIC as Receiver, Conservator, or Other Liquidator of a Failed Financial Institution (13 CFR § 120.432(a))

SBA clarified the circumstances under which it permits sales of, or sales of participating interests in, 7(a) loans. The regulation at 13 CFR § 120.432(a) applies to all 7(a) loans purchased from any Federal or state banking regulator, any receiver, or any conservator, unless SBA agrees otherwise in writing.

12. Delegated Authority Criteria for 7(a) Lenders (13 CFR § 120.440(c)

SBA made a conforming change to the delegated authority criteria regulation at 120.440(c) to clarify that a Lender's authority to participate in SBA Express may be renewed for a maximum term of 3 years (as set forth in the new regulation for SBA Express at § 120.442(c)(2)(i)).

13. 504 Loan Program Accredited Lender Program (ALP) (13 CFR § 120.840)

SBA made a technical correction to replace the reference in this section to the Director, Office of Financial Assistance with "appropriate SBA official in accordance with Delegations of Authority."

SBA also revised the reference to the ALP application process in 13 CFR § 120.840(b) in light of the modernized application submission process, which will allow CDCs to submit ALP applications electronically into the Corporate Governance Repository.

14. Conditions that apply to loans by Intermediaries to Microloan borrowers (13 CFR § 120.707)

SBA increased the maximum maturity of a loan from an Intermediary to a Microloan borrower from 6 years to 7 years.

15. Procedure for an Intermediary to get a grant to assist Microloan borrowers (13 CFR § 120.712(b) and (d))

SBA revised the regulation at § 120.712(b) to incorporate a recent statutory change to the percentage of grant funds that may be used by the Intermediary for marketing, managerial, and technical assistance to prospective Microloan borrowers. SBA revised the regulation at § 120.712(d) to incorporate a recent statutory change to the percentage of grant funds the Intermediary may use to contract with third parties to provide technical assistance to Microloan borrowers.

Questions

Questions and any comments concerning this Notice should be directed to the Lender Relations Specialist in the local SBA District Office, which can be found at https://www.sba.gov/tools/local-assistance/districtoffices.

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