U.S. Small Business Administration

Interim Final Rule (IFR)
Express Loan Programs; Affiliation Standards

Sept. 28, 2018: Proposed Rule published

Feb. 10, 2020: Interim Final Rule published

March 11, 2020: **Effective Date**

April 10, 2020: End of comment period

June 9, 2020: SBA-reviewed LSP Agreements

Oct. 1, 2020: Compliance date for Agent and 7(a) Lender fees

Where to find the rule: SBA Interim Final Rule

Dates apply to the date that SBA receives the application

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See the Interim Final Rule at:
https://www.federalregister.gov/documents/2020/02/10/2020-02128/express-loan-programs-affiliation-standards

Overview of Major IFR Changes

SBA Express and Export Express Programs (13 CFR §§ 120.441 -120.447)
Affiliation (§ 121.301(f)(4)-(7))
Personal Resources Test (13 CFR § 120.102)
Two Master Prohibition (13 CFR § 103.4)
7(a) Lender Fees (13 CFR § 120.221(a))
Agent Fees (13 CFR § 103.5(b) and (c))
Definition of Agent (13 CFR § 103.1)
Loans to Qualified Employee Trusts (13 CFR §§ 120.350 and 120.352)
504 Loan Program – Accredited Lenders Program (ALP) (13 CFR § 120.840)
Intermediaries and the Microloan Program (13 CFR § § 120.707 & 120.712(b))

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The Interim Final Rule makes 10 major changes and other small changes to program regulations.

Express Loan Programs; Affiliation Standards

- SBA Express and Export Express Programs (13 CFR §§ 120.441 -120.447)
- Affiliation (§ 121.301(f)(4)-(7))
  - Control = Affiliation
  - Current policy: SBA considers factors such as:
    - Ownership
    - Management
    - Franchise, license or other agreements/relationships
    - Identity of interest

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.

Affiliation exists when: (13 CFR § 121.301(f)(4)-(7))

One individual or entity controls or has the power to control another; or

A third party or parties controls or has the power to control both.

SBA considers factors such as ownership, management, identity of interest (close relatives, common investments, economic dependence), newly organized concerns, and franchise, license or other agreements/relationships when determining whether affiliation exists.

Note: Even though the IFR title is “Express Loan Programs; Affiliation Standards,” the IFR applies to 7(a), 504, and Microloan loan programs unless otherwise stated.

Affiliation Standards

IFR adds:

- Under “Identity of Interest:”
  - Close relatives
  - Common investments
  - Economic dependence
    - Applicants may submit agreements for SBA review of “control”
    - Guidance is available at: https://www.sba.gov/offices/headquarters/oca/spotlight
    - Through April 10, SBA is seeking comments on what constitutes “control”
- Newly organized concerns
- Totality of the circumstances

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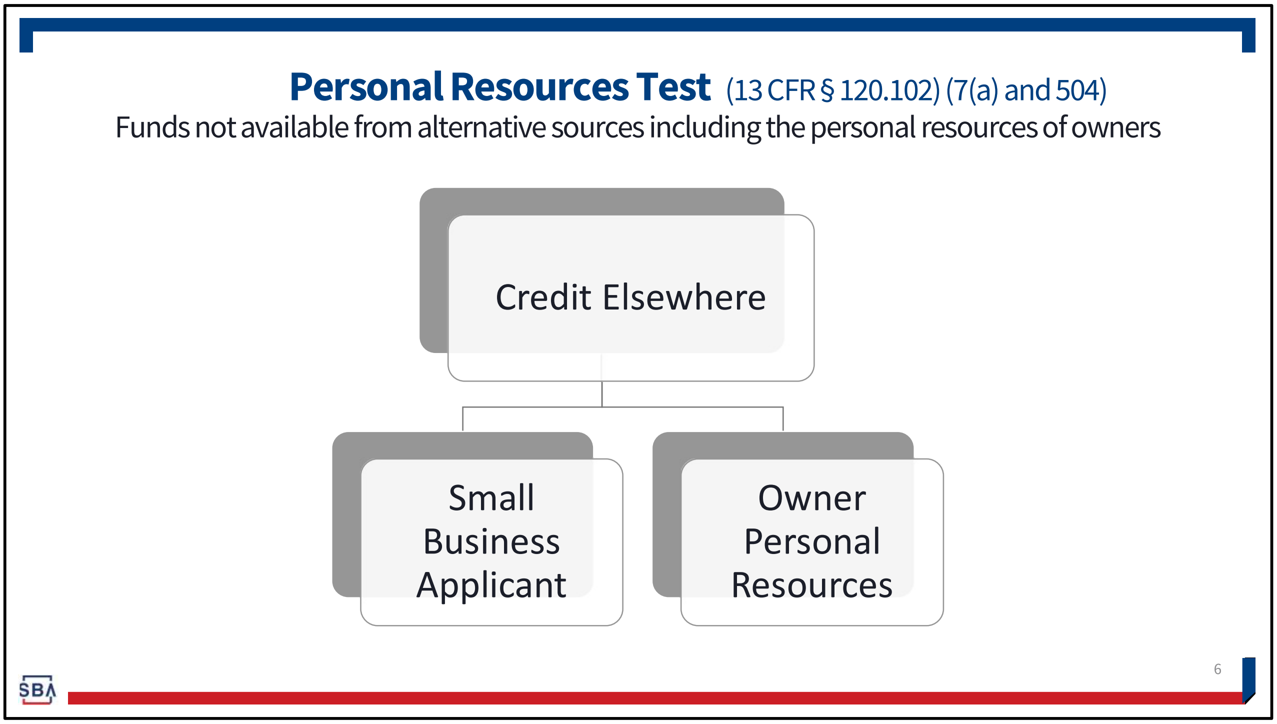
Close relatives: Affiliation arises where there is an identity of interest between close relatives, as defined in 13 CFR § 120.10, with identical or substantially identical economic interests. 13 CFR 120.10: *Close Relative* is a spouse; a parent; or a child or sibling, or the spouse of any such person.
****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.
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 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: 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.

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.

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.

* 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.



Credit not available elsewhere (13 CFR § 120.101) Current policy: SBA requires the SBA Lender to certify that the desired credit is not otherwise available on reasonable terms from non-Federal, non-State, or non-local government sources, including from the SBA Lender. The credit elsewhere provision looks at the resources of the Applicant and the owners (individuals and/or entity owners) of 20% or more of the Applicant. SBA Lenders have requested additional clarity on measuring 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.

Personal Resources Test (7(a) and 504)

When the Total Financing Package (TFP) is:	***Each*** **20%+ owner must inject liquid assets in excess of:**
$350,000 or less	2 times TFP or $500,000, whichever is greater
$350,001 - $1 million	1.5 times TFP or $1 million, whichever is greater
Greater than $1 million	1 times TFP or $2.5 million, whichever is greater

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Any liquid assets in excess of the above thresholds must be used to reduce the SBA loan amount. These funds must be injected prior to the disbursement of the proceeds of any SBA financing.

SBA Lenders must document their analysis and determination in the loan file.

Personal Resources Test (7(a) and 504)

Important Terminology:

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. loans approved within 90 days of each other) for the same project as the SBA loan.

Liquid Assets

- Cash or cash equivalents, including savings accounts, CDs, stocks, bonds, or other similar assets
- Includes the owner's spouse and any minor children
- Not liquid assets: Equity in real estate; cash value of life insurance; 401(k) plans; IRAs; 529 college savings plans; etc.

"Owners" includes individuals and entities

"at or about the same time" means loans approved within 90 days of each other

"Not liquid assets" includes assets that are tax-sheltered and subject to early withdrawal penalties such as 401(k) plans, IRAs, and 529 college savings plans

Two Master Prohibition (13 CFR § 103.4) (7(a) and 504)

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 for the same loan application

- An Agent may be both a Loan Broker *and* a Packager for the Applicant; but…
- The two master prohibition means an Agent that is a Packager for the Applicant may not also serve as a Loan Broker for the SBA Lender

7(a) Lender Fees (13 CFR § 120.221(a))

Mandatory beginning October 1, 2020: Compliance with new regulations on fees

Optional through September 30, 2020: 7(a) Lenders may choose on a per-loan basis to comply with these new limits beginning March 11, 2020

- Loans $350,000 or less: Fee may not exceed $3,000
- Loans greater than $350,000: Fee may not exceed $5,000
- Must report fees to SBA via Form 159
- No itemization required

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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.

Agent Fees (13 CFR § 103.5(b)) (7(a) and 504)

Mandatory beginning October 1, 2020: Compliance with new regulations on fees

Optional through September 30, 2020: Agents may choose to comply with these new limits beginning March 11, 2020

- 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.
- Must report fees to SBA via Form 159; All fees over $2,500 must be itemized
- Above maximums apply to the aggregate of ALL fees charged by ALL Agents to the Applicant.

Agent and 7(a) Lender Fees

For both Agents and 7(a) Lenders:

Must comply with new fee structure by October 1, 2020

Through September 30, 2020:

On a per loan basis, Agents and 7(a) Lenders may choose to comply with the new fee structures (as soon as March 11, 2020)… OR…

Continue with the same fee structure as stated in SOP 50 10 5(K)

Agent and 7(a) Lender Fees

Fee structure in **SOP 50 10 5(K) (Optional through 9/30/20)**:

- Fees may be charged on either hourly or percentage of loan basis
- If charging hourly – no maximum
- If charging on a percentage of loan:
  - Loans $50,000 or less: Fee may not exceed 3%
  - Loans greater than $50,000: 2% up to $1 million and 0.25% on the portion above $1 million; however:
  - Maximum fee charged on a percentage basis is $30,000
- Must report fees to SBA via Form 159; All fees over $2,500 must be itemized

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7(a) Lender Fees – Extraordinary Servicing Fees

(13 CFR § 120.221(b) and 120.344(b))

For EWCP and Working Capital CAPLines that are disbursed on a BBC:

- Permits extraordinary servicing fees in excess of 2% per year
- Must be reasonable and prudent
- Cannot be higher than fees charged on the Lender's similarly-sized, non-SBA guaranteed commercial loans
- Requires SBA's prior written approval

Note: The current policy on 7(a) extraordinary servicing fees remains in effect. That is, with prior SBA written approval, 7(a) Lenders may charge extraordinary servicing fees up to 2%

For Export Working Capital Program (EWCP) and Working Capital CAPLines that are disbursed based on a Borrowing Base Certificate (BBC)

Definition of Agent (13 CFR § 103.1(a)) (7(a) and 504)

"Agent" includes:

Lender Service Provider (LSP) (Applies to 7(a) Only):

- Assists the Lender with originating, disbursing, servicing, liquidating, or litigating SBA loans
- Lender bears full responsibility
- Paid only by the Lender
- LSP fees may not be passed on to Applicant or paid with SBA proceeds
- Must be operating under an SBA-reviewed LSP Agreement no later than **June 9, 2020**

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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. Note: This clarifies that the LSP may only assist the Lender (and not make decisions on behalf of the Lender)
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.

Definition of Agent (13 CFR § 103.1(a)) (7(a) and 504)

“Agent” includes:

Packager:

- Defined as an Agent who prepares the Applicant’s application for financial assistance
- Employed and compensated by the Applicant
- What is packaging?
    - Assisting the Applicant with completing applications
    - Preparing a business plan and/or cash flow projections
- Agents that provide packaging services to Lenders are considered LSPs

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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:

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

Definition of Agent (13 CFR § 103.1(a)) (7(a) and 504)

"Agent" includes:

Loan Broker (also known as Referral Agent):

May be employed and compensated by either:

- Applicant; or
- SBA Lender…

But not both

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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:

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.

Definition of Associate of SBA Lender (13 CFR § 120.10) (7(a) and 504)

<u>Definition of Associate of an SBA Lender</u>:

Revised to clarify that an Agent is an Associate of the SBA Lender

Significance:

- An SBA Lender is responsible for the conduct of its Associates
- SBA Lender must report unethical behavior of its staff and Associates to SBA
- New 7(a) Lender application requires list of Associates
- SBA Lenders and Associates prohibited from obtaining equity interest in Applicant
- SBA Lenders and Associates prohibited from having a real or apparent conflict of interest with a small business Applicant or SBA

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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:

<u>Loan Broker</u> (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.

Note: "SBA Lender" means both 7(a) Lenders and 504 Certified Development Companies (CDCs)

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

7(a) Only:

For businesses that are owned or will be owned by a qualified employee trust:

Loan to the small business concern (rather than the qualified employee trust) may be eligible if:

- Loan proceeds are only be used to make a loan to a qualified employee trust that results in the trust owning at least 51% of the small business concern

504 Loan Program ALP (13 CFR § 120.840)

Revised the Accredited Lenders Program

- Permits ALP applications to be submitted to SBA via the Corporate Governance Repository
- In case the Delegations of Authority are changed in the future, permits ALP applications to be approved by the Director of the Office of Financial Assistance or the appropriate SBA official in accordance with Delegations of Authority

Intermediaries to the Microloan Program (13 CFR § 120.707 and 120.712(b))

- Increased maximum maturity of a loan from an Intermediary to a Microloan borrower from 6 years to 7 years
- Changed the percentage of grant funds that may be used by the Intermediary for marketing, managerial, and technical assistance to Microloan borrowers.

Upcoming Training Calls & How to Subscribe

504 Connect Call March 24, 2020 at 3:00 Eastern
Register at: https://ems8.intellor.com?do=register&t=1&p=820100

7(a) Connect Call April 7, 2020 at 3:00 Eastern
Register at: https://ems8.intellor.com/?do=register&t=1&p=820109

OFASubscribe@sba.gov Subscribe/unsubscribe to 7(a) and/or 504 calls, trainings, and updates (Please state if for 7(a), 504, or both)

Please whitelist SBAConnect@sba.gov and noreply@event-services.com to ensure that you receive your unique login instructions.

Personal Resource Test (7(a) and 504)

Effective Date 3/11/2020

Maximum Liquid Assets for Each 20% Owner – Based on Total Financing Package (TFP)			
Total Financing Package	**(TFP) is <= $350K:** Maximum liquid assets for each 20% owner: **2 X TFP amount or $500K whichever greater**	**TFP is $350,001K - $1MM:** Maximum liquid assets for each 20% owner: **1.5 X TFP amount or $1MM whichever greater**	**TFP > $1MM:** Maximum liquid assets for each 20% owner: **1 X TFP amount or $2.5MM whichever greater**
$100,000	$500,000 **A**		
$350,000	$700,000 **B**		
$500,000		$1,000,000 **C**	
$1,000,000		$1,500,000 **D**	
$1,500,000			$2,500,000 **E**
$3,000,000			$3,000,000 **F**

A: $100,000 TFP x 2 = $200,000; but allowed up to the maximum of $500,000
B: $350,000 TFP x 2 = $700,000
C: $500,000 TFP x 1.5 = $750,000; but allowed up to the maximum of $1MM
D: $1MM TFP x 1.5 = $1.5MM
E: $1.5MM TFP x 1 = $1.5MM; but allowed up to the maximum of $2.5MM
F: $3MM TFP x 1 = $3MM

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Total Financing Package (TFP) is defined as 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. loans approved within 90 days of each other) for the same project as the SBA loan.

When calculating an owner’s liquid assets, begin with the personal financial statements provided at loan application and subtract out any equity injection to be made for the project.