

### 3. What are Counsel's Responsibilities for Direct Loan Closings?

You, as SBA Counsel, are responsible for:

- a. Preparing loan closing documents;
- b. Conducting the loan closing;
- c. Perfecting SBA's security position; and
- d. Authorizing the disbursement of direct loans.

### 4. What are Counsel's Responsibilities for 504 Loan and Debenture Closings?

- a. Who is Responsible for Closing the 504 Loan and Debenture?

The CDC Counsel is responsible for all actions, document preparation, and other procedures necessary to close each 504 loan, in compliance with all 504 loan program requirements, which include requirements imposed upon the CDC by statute, SBA regulations, any agreements between the CDC and SBA, SBA SOPs, official SBA notices and forms applicable to the 504 loan program, the debenture, and the loan authorization. Although SBA Counsel is available for advice and assistance, the CDC and its attorney are ultimately responsible for 504 loan closing. Policy and procedures for 504 closing and handling of documents post closing are outlined in SOP 50 10.

Responsibility for closing the 504 debenture is jointly held by the CDC Counsel and SBA Counsel. CDC Counsel must prepare the documents necessary for closing the debenture. The CDC and CDC Counsel must ensure that the documents the CDC uses to close the 504 loan do not conflict with the documents in the debenture closing package. SBA Counsel reviews the debenture closing documents for legal sufficiency and determines whether SBA may guarantee the debenture.

- b. What Are the Types of Debenture Closing Packages?

There are two types of debenture closing packages, a regular closing package submitted by either a CDC not approved for participation in the expedited closing procedure described in SOP 50 10 or a Priority CDC not using a designated attorney, and an expedited closing package submitted by a Priority CDC and its designated 504 loan closing attorney under the expedited closing procedure.

- c. What Does a Debenture Closing Package Include?

SBA has adopted a standard 504 Debenture Closing Checklist (Checklist) (SBA Form 2286). CDCs and SBA must use this 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.

For regular closing packages, SBA requires that the CDC submit only the 12 items on the Checklist to SBA for SBA's review at closing. For expedited closing packages, SBA requires that the CDC submit only the first seven items on the Checklist to SBA for SBA's review at closing. In either type of closing package, the CDC may submit additional

documents, provided that the CDC includes an analysis and discussion of the significance of such additional documents to the debenture closing and why SBA should review such documents as part of its review of a particular debenture closing package.

The documents on the list that have an SBA form number are mandatory forms; the CDC must not substitute its own forms for those documents. In addition, use of the boilerplate form of the Opinion of CDC Counsel (Appendix D to the 504 Authorization Boilerplate) is mandatory. While the CDCs may use their own forms for the lien instruments on project property and security agreement, those forms must be either state bar approved forms or be approved by SBA Counsel prior to submission.

The following are the 12 documents on the Checklist:

1. CDC Board Resolution (SBA Form 1528)
2. Note (CDC/504 Loans) (SBA Form 1505)
3. Development Company 504 Debenture (SBA Form 1504)
4. Servicing Agent Agreement (SBA Form 1506)
5. CDC Certification (SBA Form 2101)
6. Opinion of CDC Counsel (Appendix D to the 504 Authorization Boilerplate)
7. Evidence of priority of liens on Real and Personal Property (title insurance; UCC filings and search)
8. Unconditional Guarantee (SBA Form 148 or 148L)
9. Lien instrument on Project Property
10. Assignment of lien instrument on Project Property
11. Security agreement for Project Property with assignment
12. Secondary collateral (lien instruments; assignments)

d. How Must the CDC Complete Each Closing Document on the Checklist?

To properly complete the debenture closing documents listed on the Checklist, for SBA review, follow the instructions for each item listed below:

The 504 Debenture Closing Checklist (SBA Form 2286) must be submitted with each closing package, and the copies of debenture closing documents must be submitted in the order set forth in the Checklist.

- (1) CDC Board Resolution (SBA Form 1528): The CDC Board Resolution must set forth the correct Borrower(s) name and the Debenture Amount must be equal to or greater than the amount on the closing documents and the Authorization, as amended, at the time of debenture closing.
- (2) Note (CDC/504 Loans) (SBA Form 1505): The Note must have a date that does not pre-date the Authorization. See the Instructions for Use of SBA Form 1505, 504/CDC Note for detailed instructions on completing the Note.
- (3) Development Company 504 Debenture (SBA Form 1504). An authorized representative of the CDC must sign the debenture.
- (4) Servicing Agent Agreement (SBA Form 1506): The Use of Project Proceeds and Sources of Funds must conform to the Authorization, as amended. If the amounts or percentages have changed since loan approval, the CDC must request, before submission of the debenture closing package, a modification to the Authorization to

show the final actual amounts. The fee information must be accurate. The wire instructions must be complete. All Borrowers and Operating Companies must sign.

(5) CDC Certification (SBA Form 2101): The CDC must use SBA's standard form.

(6) Opinion of CDC Counsel (Appendix D to the 504 Authorization Boilerplate) must:

- Conform to Appendix D of the Boilerplate.
- Reflect appropriate review of all closing documents.
- Contain accurate project financing amounts and lien positions that conform to the Authorization and the Servicing Agent Agreement.
- Include Paragraphs D.6-D.8 opining on the Borrower and Operating Company's proper organization, authority to execute the documents, and the validity and enforceability of documents signed by the Borrower and Operating Company. CDC Counsel may reference and rely on an Opinion from Borrower and/or Guarantor's Counsel.
- Be signed by the CDC Counsel.
- Include a copy of the SBA approval to use Option C, if that option is being used for an out-of-state project.
- CDC Counsel may represent the Third Party Lender provided the required waivers are obtained from the CDC and Third Party Lender and CDC Counsel makes the certifications as set forth in the relevant paragraph, which must be included in the Opinion of Counsel.

(7) Evidence of priority of liens on real and personal property collateral: For real property, the CDC and CDC Counsel must submit an ALTA title policy unless SBA counsel approves the submission of a commitment. In states where ALTA policies are not available, the CDC and CDC Counsel must provide the appropriate insurance commitment or policy. A title policy must cover both the CDC and SBA, properly identify the covered lien and any exceptions to coverage, confirm that SBA's lien position conforms or will conform to the Authorization after the payoff of the Interim Financing, have no exceptions for mechanic's liens or provide coverage over these liens, and remove the "liability non-cumulative" or "cumulative payment" clause (unless the CDC uses a different title company than the Third Party Lender). Commitments must be marked-up or accompanied by closing instructions indicating that all these requirements will be met in the final policy, and must have a specific date and not state "date of recording." For personal property, the UCC financing statement must be filed and a UCC lien search done revealing SBA is in the lien position required by the Authorization subject to the payoff of the Interim Financing.

(8) Unconditional Guarantee (SBA Form 148 or 148L): Guarantees must be signed by the individuals and/or entities required in the Authorization, each in their proper capacity. If a limited guarantee is required, the limitation stated on the guarantee must match the language in the Authorization. The date on the Guarantee must not pre-date the Note.

(9) Lien instrument on Project Property: The instrument must contain the Federal Law language required by the Authorization, even if the SBA form is used.

(10) Assignment of lien instrument on Project Property.

- (11) **Security agreement for Project Property:** If the CDC is using its own form of security Agreement, it must contain the Federal Law language required by the Authorization. If the CDC is using the SBA Security Agreement (SBA Form 1059), it must be the version dated 2-2004. Previous versions of the SBA Form 1059 are obsolete and are not acceptable. The security agreement must be assigned to SBA.
- (12) **Secondary collateral:** The CDC must submit lien instruments related to any non- project property that is secondary collateral required by the Authorization, such as a home mortgage that secures a personal guaranty. These documents must be assigned to SBA. See the instructions for lien instruments on real property, security agreements and UCC-1 financing statements for personal property, above.

e. What are SBA Counsel's Specific Responsibilities for 504 Closings?

- (1) Issue an annual 504 debenture closing schedule with District Office deadlines for receiving closing packages. SBA Counsel responsible for debenture closing in each District Office must make available to the public an annual schedule of the deadlines for receipt of closing packages for each monthly debenture sale. The schedule must include submission deadlines for both regular closings and expedited closings. The District Office must disseminate the schedule to the CDCs that regularly submit closing packages to that district office as well as make it publicly available to any other interested CDCs through the District Office website or similar method.
- (2) Review closing packages. SBA Counsel must use the standard Checklist to review the closing package and generally must not require CDCs to provide documents not on the Checklist. 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. SBA Counsel must use the column labeled "SBA" on the Checklist when reviewing the debenture closing package, and check off each document as it is reviewed. Refer to the instructions accompanying the Checklist for guidance on what SBA Counsel must review for each item on the Checklist. SBA Counsel may rely upon the facts stated in the CDC Counsel Opinion and the CDC Certification when reviewing the closing package, but must be satisfied from a review of the package that the CDC has closed the 504 loan in compliance with all 504 loan program requirements, which include requirements imposed upon the CDC by statute, SBA regulations, any agreements between the CDC and SBA, SBA SOPs, official SBA notices and forms applicable to the 504 loan program, the Debenture, and the Authorization. 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.
- A. Reviewing closing packages submitted by Non-Priority CDCs or by a Priority CDC not using a designated attorney: SBA Counsel must review all 12 documents submitted with the Checklist.
- B. Reviewing closing packages submitted by Priority CDCs using a Designated attorney: SBA Counsel must review only the first seven documents on the Checklist. If SBA Counsel's review indicates that there is a reasonable basis for the conclusions reached by the CDC or the designated 504 closing attorney in

preparing the loan and debenture for closing and sale, SBA Counsel will accept those conclusions and will not substitute his or her own judgment.

- (3) 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.
- (4) 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 C.F.R. §120.960(c) stating that the debenture may be closed, SBA may execute its guarantee, and the debenture may be sold. The standard format for the SBA Counsel opinion is in Appendix 4d. The SBA Counsel's Opinions should be sent to the SLPC.
- (5) 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 District Office approves for funding in that month's sale.
- (6) Conduct quality assurance reviews (QAR) of closing packages submitted by Priority CDCs and selected for QAR. SBA Counsel must perform a QAR of a random selection of the closing packages submitted by Priority CDCs, following the procedures in paragraph 5 of this chapter.
- (7) Conduct complete file reviews of 504 loan and debenture closings. SBA Counsel must perform a complete file review of a random selection of 504 loan and debenture closings, following the procedures in paragraph 5 of this chapter.

## **5. Quality Assurance Reviews (QAR) of Priority CDC Closings, and Complete File Reviews of Closings**

### **a. QARs of Expedited Closings.**

#### **(1) Purpose and frequency of QARs.**

SBA Counsel must conduct QARs of a random selection of closing packages submitted by Priority CDCs for purposes of assuring the quality of the expedited closing process. For each designated 504 closing attorney, each quarter, SBA Counsel must review closing packages representing ten (10%) per cent of loans closed by such attorney that quarter or one loan, whichever is greater

## (2) What is a QAR of an expedited closing package?

A QAR of an expedited closing package submitted by a Priority CDC is a review by SBA Counsel of the closing package as if it were a regular closing package

submitted by Non-Priority CDCs as described in paragraph 4 of this chapter (including a review of all 12 documents that would have been required to be included in the package if it had been a regular closing package). SBA Counsel also may review the basis for the designated 504 closing attorney's decisions and risk assessments. SBA Counsel must determine whether the loan and debenture were closed in accordance with 504 loan program requirements, including without limitation SBA regulations and policies and the Authorization; the required collateral and lien positions were obtained; and the designated 504 closing attorney's opinion accurately reflected the legal status of the documents and the closing.

## (3) Procedures for QARs.

SBA Counsel must perform the QAR after the date the CDC sent loan closing documents to the CSA for debenture sale. SBA Counsel must identify for the Priority CDC the loans for which the CDC must submit a regular closing package (in other words, for which the CDC must submit the remaining seven documents on the Checklist that the CDC did not already submit as part of the expedited closing package), and provide the CDC with until the close of business on the third business day after SBA Counsel's request to submit the package. SBA Counsel must prepare a written report documenting the QAR and its results. SBA Counsel must send a copy of the QAR report to the CDC and its designated 504 closing attorney, as well as to the Department of Financial Law and Lender Oversight in the Office of General Counsel, the Office of Credit Risk Management (OCRM), the Sacramento Loan Processing Center and the appropriate Commercial Loan Servicing Center. SBA Counsel also must file a copy of the QAR report in the district office's file regarding that CDC.

## b. Complete File Reviews of 504 Loan and Debenture Closings.

## (1) Purpose and frequency of Complete File Reviews.

SBA Counsel must review a random selection of all 504 loan and debenture closings, whether those closing packages were submitted by Priority CDCs or non-Priority CDCs, for purposes of ensuring program integrity in the 504 loan and debenture closing process. The number and frequency of Complete File Reviews are at the discretion of SBA Counsel, determined in conjunction with the Department of Financial Law and Lender Oversight in the Office of General Counsel, provided that for each CDC submitting closing packages to a particular District Office, no less than one package per 20 closing packages submitted by that CDC to that District Office are audited.

## (2) What is a Complete File Review of a 504 loan and debenture closing?

A Complete File Review of a 504 loan and debenture closing is a review by SBA Counsel of the CDC's entire 504 loan and debenture closing, consisting of all of the

CDC and CDC Counsel's decisions and risk assessments. SBA Counsel must determine whether:

- The loan and debenture were closed in accordance with 504 loan program requirements, including without limitation SBA regulations and policies and the Authorization;
- The required collateral and lien positions were obtained;
- The file contains sufficient documentation in support of the representations made by the CDC and its counsel in the CDC Certification and the Opinion of CDC Counsel during the closing;
- Any evidence in the file calls into question the accuracy of any of those representations;
- Any evidence in the file should have caused the CDC, upon whose professional judgment SBA relies to evaluate as part of closing the potential and likelihood of financial loss under the 504 loan or debenture, to conduct further inquiry before closing the loan and debenture and submitting the debenture for sale (for example, evidence indicating a substantial adverse change in Borrower's financial condition after loan approval), and the CDC failed to do so;
- The CDC Counsel's legal opinion accurately reflected the legal status of the documents and the closing; and
- Any other issues or concerns exist that would affect program integrity.

(3) Procedures for Complete File Reviews.

SBA Counsel must perform the Complete File Review after the date of debenture sale. SBA Counsel must identify for the CDC the loans for which the CDC must submit a copy of its loan and debenture closing file, and the CDC must submit the package no later than the close of business on the third business day after SBA Counsel's request to submit the package SBA Counsel must prepare a written report documenting the Complete File Review and its results. SBA Counsel must send a copy of that report to:

- The CDC that submitted the closing,
  - The CDC's 504 closing attorney that closed the loan and debenture,
  - Department of Financial Law and Lender Oversight in the Office of General Counsel,
  - OCRM,
  - The Sacramento Loan Processing Center, and
  - The appropriate Commercial Loan Servicing Center.
- SBA Counsel also must file a copy of the report in the loan file and in the district office's file regarding that CDC.

c. What happens if SBA Counsel finds deficiencies in conducting a QAR or Complete File Review (referred to collectively as "review")?

(1) Minor deficiencies. If the review reveals minor deficiencies in the CDC's loan and debenture closing, SBA Counsel will request that the CDC and its closing attorney correct the deficiencies and make any necessary changes to their loan closing process so that such deficiencies do not recur.

(2) Significant deficiencies. If the review reveals any deficiencies that might result in a loss to SBA, SBA Counsel must request that the CDC and its closing attorney correct the deficiencies with the loan documents, if possible, and provide information to show that changes have been made to their loan closing process so that such deficiencies do not

recur. Additionally, it is generally expected that SBA Counsel will initiate one or more of the following corrective actions:

- (a) Take steps to protect SBA's interests under that particular debenture including, without limitation:
  - Advising the CSA that the debenture may not be sold in that month's debenture sale (pursuant to 13 C.F.R. 120.960(c)) if such sale date has not yet passed; and
  - Advising the CDC that pursuant to the terms of the debenture, the limitation on SBA's recourse against the CDC itself for any default under the debenture may be of no force and effect due to the CDC's negligence in a material aspect of the transaction; and
- (b) Increase the number and frequency of reviews SBA Counsel performs on closings submitted by that CDC and/or its closing attorney.
- (c) Recommend that OGC place the designated 504 closing attorney on probation or suspend the attorney for a period of time not to exceed six months, during which time the attorney must submit regular closing packages to that District Office as if it represented a non-Priority CDC, and SBA Counsel will review such packages using the procedures applicable to regular closing packages submitted by non-Priority CDCs.
- (d) Recommend to OGC that the designated 504 closing attorney's status be withdrawn for good cause pursuant to SOP 50 10, SUBPART H, Chapter 22, paragraph 7.g.
- (e) Recommend that SBA suspend or revoke the CDC's priority status, if applicable.
- (f) Refer the matter to the Office of Credit Risk Management (OCRM) to determine whether additional 504 program oversight or enforcement action against the CDC, as described in SBA policies and regulations, is appropriate.
- (g) Take any other action appropriate to protect SBA's interest, including, but not limited to, asserting a claim against CDC counsel's malpractice insurance.
- (3) If CDC or closing attorney is not cooperative with an SBA Counsel's request, counsel should refer the CDC or closing attorney for consideration of suspension or other corrective action.

**6. Are There any Conflicts of Interest Issues that SBA Counsel Must Consider Regarding Closing Attorneys?**

- a. Because of potential conflict of interest issues, you must consider the relationship between a CDC and an attorney.
- b. In the following relationships between an attorney and a CDC, the attorney is considered, as a matter of policy, not to be independent:
  - (1) A CDC's in-house Counsel; and

- (2) An attorney employed by a state or municipal CDC, or a governmental affiliate of the CDC.

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