



SBA Information Notice

TO: All SBA Employees

CONTROL NO.: 5000-1322

SUBJECT: Clarification of the Ineligibility of
Certain Passive Business Models

EFFECTIVE: 10-10-2014

The Agency defines certain personal services businesses with the following descriptions as eligible in SBA's Standard Operating Procedure (SOP) 50 10 5(G):

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

These eligible barber shop, hair salon and nail salon applicants employ individuals and/or retain the services of an independent contractor to provide services. The public perception is that there is only one business, operated by the business owner. The individual service providers, who are either employees or contractors, work together in common space and use shared services (e.g., shampoo and other salon services) provided by the business owner, for which the business owner may or may not charge a fee. This is in contrast to the “salons suites” model where the business owner collects rent and each individual service provider leases space that is an identifiable, self-contained private space utilized only by that third party provider.

SBA has recently reviewed several franchised businesses that use the “salons suites” concept, where the business seeks funds to make significant alterations to space acquired through purchase or lease, in order to create identifiable, self-contained private spaces for lease to independent third party businesses that provide personal services. These personal services are typically beauty, barber, or similar personal services.

Agency regulations define certain types of businesses as ineligible for SBA financial assistance including the following:

“Passive businesses owned by developers and landlords that do not actively use or occupy the assets acquired or improved with the loan proceeds (except Eligible Passive Companies under 120.111).” (13 CFR 120.110(c))

Certain franchised “salons suites” business models recently brought to SBA's attention are structured for the franchisee to lease most or all of the space acquired and/or renovated with loan proceeds to third party tenants. This “salons suites” business model generates income by renting space to accommodate independent businesses that provide the personal services.

Under this business model, the franchisee (whether an owner or renter of the real estate) typically maintain grounds, hallways and restroom facilities, with tenants responsible for maintaining their individually-leased suites. The provider of the space openly advertises the concept as a place to receive identified personal services, but the individual business tenants may also advertise

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independently. Customers entering the location see a facility which contains multiple independent operators providing personal services. Related merchandise may be offered for sale by the individual tenants, but generally not by the provider of the leased space. In some facilities, however, there are limited products sold at the common entrance.

SBA considers business models which demonstrate these characteristics to be passive businesses and ineligible under the regulation at 13 CFR 120.110(c). When an applicant for financial assistance is in the business of maintaining and renting space to other businesses, it is a landlord and not eligible for an SBA guaranty. This is true whether or not the applicant operates a franchise or non-franchise business.

As additional clarification, SBA policy has long stated that the applicant business must occupy a majority (51% or more) of the space it acquires/renovates with SBA proceeds. (13 CFR 120.131) While some third party leased space is permitted, loan proceeds may not be used to improve space leased to third parties. In SBA's review of some "salons suites" business models, a majority of requested loan funding would be used for construction or renovation of the individual suites, which are then rented to individual service providers. Such use of proceeds would be ineligible.

SBA is providing this guidance to ensure that SBA loans are made only to eligible small businesses and that the SBA-guaranteed loan proceeds are approved only for eligible purposes. SBA will continue to review such business models when presented, and will work with lenders, applicants, and where applicable franchisees and franchisors to assist in providing any needed clarifications.

Notification and Questions:

SBA field offices are responsible for notifying its participants about the clarifications outlined in this Notice. SBA field offices with questions on this notice may direct them to Dianna Seaborn at dianna.seaborn@sba.gov in the Office of Financial Assistance. Lenders are directed to forward questions to their local SBA field office. A list of the local SBA field offices may be found at: www.sba.gov/localresources/index.html.

Linda S. Rusche, Director
Office of Financial Assistance