



# SBA Information Notice

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**TO:** All SBA Employees

**CONTROL NO.:** 5000-1163

**SUBJECT:** Issuance of SOP 50 10 5(C) – Lender  
and Development Company Loan  
Programs

**EFFECTIVE:**  
**9/7/2010**

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The Office of Financial Assistance is announcing the issuance of an update to the Standard Operating Procedure (SOP) 50 10 5. This update to the SOP will be known as SOP 50 10 5(C) and will be effective on October 1, 2010. This version of the SOP will apply to all applications received by SBA on or after October 1, 2010.

As with previous editions of SOP 50 10 5, SBA will post two versions on the web site. The first version will show all changes as “tracked changes” to enable users to more easily identify what has been modified. (As a note, the Table of Contents has been updated but, for ease of viewing, those changes are not shown.) The second version incorporates all of the changes into the document. The revised SOP may be found at <http://www.sba.gov/aboutsba/sbaprograms/elending/reg/index.html>.

The following is a summary of the key changes made to this version of the SOP. Many of the changes are in response to questions and comments received from lenders and CDCs through the SOP mailbox or through the district offices and processing centers. The changes identified below fall into two categories: simplification and risk management.

Changes Resulting in Simplification of the Loan Application Process including Expanding the Definition of Eligible Small Businesses and Expanding the Eligible Uses of Proceeds

- a. **Passive Income Definition:** The definition has been modified to recognize changes in the business model for many types of businesses. This modification results in a more simplified definition that will permit more small businesses to be eligible for an SBA guaranteed loan. Until recently, businesses such as hair salons, nail salons, dance studios and others would typically hire the trades people that provided the services as employees. Now, many rent space to the tradesperson and then handle advertising, hiring cleaning services and the sales of merchandise. Under the previous guidance, these businesses were ineligible for SBA financing unless more than 50% of their revenue was from sources other than rent (the “sufficient services” test). The new guidance eliminates the “sufficient services” test in order to make SBA loan guarantees available to more of these types of businesses.
- b. **OREO transactions:** Historically, a 7(a) lender could not finance Other Real Estate Owned (OREO) with a 7(a) loan because SBA perceived this as self-dealing. Based on numerous requests from 7(a) lenders to permit these same lenders to finance their OREO

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property with a 7(a) loan, SBA identified what it believes are sufficient controls to permit this type of financing while eliminating an actual or apparent conflict of interest. The SOP has been modified to permit the financing of OREO property as long as the application is submitted to the appropriate SBA processing center for a decision by SBA and the application meets certain stated conditions. The same conditions that will now apply to applications submitted under 7(a) have also been added to the 504 Loan Program, where lenders have traditionally been permitted to act as a third party lender for their OREO property. This will tighten the guidance in the 504 program to provide stronger risk management and provide consistency between the two programs.

- c. Interest Rate changes between application and first disbursement: Previously, the SOP required the interest rate to remain fixed until the first adjustment date identified in the note. In response to numerous requests from lenders as well as SBA's servicing centers, the SOP has been modified to permit a lender to reduce the interest rate after loan approval and prior to first disbursement as long as the borrower agrees in writing.
- d. Debt refinancing: SBA has clarified a section of the SOP dealing with debt refinancing and partial change of ownership situations. The SOP has been revised to more clearly state that if a loan will be used to finance a partial change of ownership and also refinance the existing debt of the business, then the debt refinancing provisions do apply and need to be met in order for the application to be eligible.
- e. EWCP: The SOP has been revised to include an expanded version of the sections of the SOP dealing with the Export Working Capital Program. The additions will clarify how this particular program should be used.
- f. Amortization of Third Party Loan (TPL): This provision has been modified to permit the TPL to begin amortizing prior to the funding of the 504 loan as long as the borrower has provided his/her written consent.
- g. Exception to Policy Authority: Language has been added to the SOP, at the beginning of each Subpart, to clarify the Director of the Office of Financial Assistance's authority to consider and make a decision on requests for an exception to a policy with respect to a particular loan request.
- h. 504 Borrowed Equity: The treatment of borrowed equity in 504 loans has been revised to state that "If the borrowed equity is collateralized by assets other than the Project Property, the borrower must demonstrate repayment of the loan for the equity contribution from the cash flow of the business or other sources." Previously, the repayment of borrowed equity was not considered in the cash flow analysis of the business.
- i. Public Policy Goal: Guidance has been added concerning the use of a military base closing as a public policy goal to permit a larger loan. The SOP has been revised to require the CDC to submit additional documentation if the base closure is more than 10 years in the past.

- j. Small/Rural Lender Advantage: The S/RLA process has been modified to reduce the two tiers of analysis to only one tier. This change will streamline and simplify the S/RLA process.

#### Changes that Seek to Improve SBA's Management of Risk

- k. Source of Equity and documentation: The guidance on the permissible sources of equity and documentation of equity injection has been expanded and moved from SOP 50 51 (which deals with purchases and liquidations) to SOP 50 10. As a result, lenders will be aware of what SBA requires regarding documentation of equity injection prior to closing and disbursing a loan.
- l. Business Acquisitions: The following revisions have been made: (1) tightening up the requirements concerning who is qualified to perform a business valuation; (2) changing the timing of the requirement to obtain a business valuation to before the application is submitted to the LGPC or, for applications processed under delegated authority, after receipt of the SBA loan number but prior to closing; (3) adding a statement that any difference between the sales price and the business valuation may not be financed with the SBA-guaranteed loan; and (4) adding language to require the lender to verify the financial information relied upon in the business valuation.
- m. Delegated Lender Criteria: The initial approval and renewal criteria for delegated authority have been revised in order to have more consistency from program to program. In addition, language has been added to the CLP approval/renewal process discussion that requires the lender to continue to meet the requirements of 120.410, including adequate capitalization. Finally, the PLP-EWCP approval process has been revised.
- n. SBA Form 912: The language in the SOP regarding who must complete SBA Form 912 has been amended to: (1) add "any person hired by the Applicant to manage day-to-day operations" (i.e., "key employee"); (2) address which members of a Limited Liability Company (LLC) must complete a 912 (each member owning 20% or more of the LLC, and each officer, director and managing member); and (3) clarify which partners of a partnership are required to complete a 912 (each general partner and all limited partners owning 20% or more of the partnership).

#### Miscellaneous Changes

- o. Language defining job creation and retention has been added to the 7(a) subpart and the definition of "job opportunity" has been revised in the 504 subpart. Due to the nature of the two programs, there is a slight difference in the definitions.
- p. Interest rate swaps: A description of interest rate swaps has been added to the SOP that allows the use of interest rate swaps under certain conditions.

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Additional Information

Lenders, CDCs and other interested parties may continue to send suggestions concerning the SOP to SBA at [SOP50-10Modernization@sba.gov](mailto:SOP50-10Modernization@sba.gov). This e-mail box is set up to receive only.

Questions regarding SOP 50 10 5(C) should be directed to the lender relations specialist in the local SBA field office. The local SBA field office may be found at [www.sba.gov/localresources](http://www.sba.gov/localresources).

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