



Lender Consent Questions & Answers: April, 2001

1. INTRODUCTION

In 1999, the SBA initiated an innovative program to reduce the balance of SBA-held loans by up to \$10 billion over a three-to-four-year period, under a government-wide initiative to sell federal loan assets to the private sector. The SBA plans to sell at least \$1 billion in loans under this program annually. Since its first sale in August 1999, the SBA has conducted three highly successful sales of loans from its Section 7(a), Development Company, and Disaster Assistance loan programs.

To assist lenders in determining whether to consent to including their portions of the 7 (a) or 502 loans in SBA asset sales, the SBA is providing answers to frequently asked questions concerning the process.

2. GENERAL QUESTIONS

2.1 Why is SBA selling its portfolio of direct loans and purchased guaranteed loans?

The Small Business Administration is reinventing itself as a 21st Century leading edge institution. SBA intends to reallocate staff away from some direct loan management functions. This will allow the staff to oversee and monitor the lender's process of originating and servicing loans and the quality of the loans that are created. Loan asset sales are one part of the reinvention process.

2.2 What were the results of the first three sales?

2.2.1 Sale #1

Sale #1, bid in August of 1999, consisted of 4,060 small business loans that the SBA had either made directly or had previously guaranteed for private sector lenders were sold. The unpaid principal balance ("UPB") of the loans included in the sale totaled approximately \$332 million, with about half the loans classified as non-performing or under-performing.

The loans were divided into 26 different loan pools to maximize value. The SBA received 135 bids from 25 different bidders. The winning bids varied widely based on the characteristics of the various loan pools.

2.2.2 Sale #2

Sale #2, bid in August of 2000, included 26,283 direct and guaranteed loans made under the 7(a), Development Company and Disaster Assistance loan programs. The UPB for the performing and non-performing loans included in the sale totaled approximately \$1.2 billion. SBA received 203 bids from 14 different bidders for the 75 different loan pools.

The loan pools were sold to three purchasers for approximately \$530 million. Approximately 13.5% of the loans were 7(a) and Development Company loans with the remainder being Disaster Assistance loans. The Disaster Assistance loans were low

coupon, approximately 4%, and long term, approximately 20 years remaining. Almost 26% of the UPB of these loans were located in territories or states outside the Continental United States. The largest concentration was Guam with approximately 9% of the UPB of the total portfolio.

2.2.3 Sale #3

Sale #3, bid in December of 2000, included 19,033 direct and guaranteed loans made under the 7(a), Development Company and Disaster Assistance loan programs. The UPB's for the performing and non-performing loans included in the sale totaled approximately \$1.13 billion. SBA received 100 bids from 15 different bidders for 46 different loan pools. Approximately 9% of the loans by UPB were 7(a) and Development Company loans with the remainder made up of Disaster Assistance Home and Business loans.

2.3 Will lender-serviced Section 7(a) loans be sold in future sales?

The largest portion of the Section 7(a) "SBA-owned portfolio" is now lender-serviced because the SBA has moved more of the servicing responsibilities for purchased guaranteed Section 7(a) loans to the lenders in recent years. In order to implement the mandate from the U.S. Congress to sell all SBA-owned loans, the Agency will continue to work with its lending partners to include these loans in future sales.

2.4 What happens to the lender's interests in Section 7(a) loans that are sold by the SBA?

The lender's interests will be sold along with the SBA's interests.

2.5 Why should lenders include their loans in Sale #5?

Lenders can be assured that the loan sales will be conducted in a commercially reasonable manner. The SBA conducts competitive solicitations and engages qualified private sector sales contractors.

A Program Financial Advisor has been retained to oversee development and implementation of the Loan Sale Program. A Transaction Financial Advisor is hired for each sale to market and sell the specific loans identified for the sale. A Due Diligence Contractor is employed to provide full disclosure to potential investors, and a Legal Advisor is retained to assist in developing legal documents and addressing legal issues associated with selling the loans. These sales contractors are experienced in both private sector and federal government loan sales. Additionally, SBA uses the latest electronic technology to disseminate information to prospective bidders.

Lenders will not bear the costs of the Program Financial Advisor or the SBA staff. The SBA covers the overhead costs associated with the Loan Sale Program, and deducts only the direct costs of each sale from the gross sales proceeds.

2.6 What happens if a lender does not want to sell its interest in a purchased Section 7(a) Loan?

The SBA believes that a whole loan sale will result in higher proceeds to both the SBA and the lenders. However, the SBA may seek the lender's consent to sell only the SBA's participated share. At that time to maximize value, separate pools of participated loans containing only the SBA's interest will be created.

2.7 *Can a lender purchase the SBA portion of loans in which the lender also owns a portion before the loans are offered for sale?*

Lenders can purchase the SBA portion at par at any time prior to the Bid Date. Absent that, the SBA believes that a full, open, and competitive sale will generate the best overall return. The SBA cannot sell the loans to the lender at a discount except through a competitive bidding process.

2.8 *Will borrowers have an opportunity to purchase their own loans at a discount prior to the SBA offering the loans for sale?*

No. The SBA believes that a full, open, and competitive sale will generate the best overall return. During the due diligence process, borrowers will be notified that they may prevent their loan from being sold by paying the full outstanding principal balance plus accrued interest.

2.9 *Will the SBA be seeking the approval of lenders to sell the Section 504 loans?*

No. The Section 504 loans are structured differently than the loans requiring lender approval. Rather than one loan made by the lender and guaranteed by the SBA, there are two distinct obligations. The lender has a senior lien on the collateral securing their loan and the Development Company has the junior lien. The Development Company obligation carries the SBA guarantee and once the guarantee has been honored, there is generally no continuing ownership interest by the Development Company. The SBA-owned debt can then be sold without any further approvals from the parties. In rare instances where the Development Company retains an ownership interest, the Development Company's consent to sell the loan will be requested.

2.10 *Where can questions about the sales or servicing procedures be directed?*

2.11.1 Sales Procedures: lenderquestions@sba.gov

2.11.2 Servicing Procedures: Your SBA Field Office contact is available to help you.

2.11 *How will SBA correspond with lenders throughout the sale to provide general instructions?*

The SBA will periodically distribute notices to the lenders. These notices may contain answers to frequently asked questions, an update of the status of the sale, and/or additional instructions for the lenders. If the notice can be sent to an e-mail address, please provide this information on the Lender Questionnaire (Attachment IV), along with a contact name, mailing address, phone number and fax number. Lender updates will also be posted on the SBA's external website, <http://www.sba.gov/assets/lenderscorner.html>.

2.12 *Will borrowers be notified that their loans are being sold?*

The SBA will notify borrowers that their loan(s) are scheduled to be sold once the applicable lender's consent is obtained. The SBA's experience in previous sales was that the notice to the borrower resulted in a number of loan payoffs and compromises. The SBA expects this trend to continue in Sale #5. The SBA has no legal obligation to notify business loan borrowers that their loans will be sold. As part of the SBA's continuing commitment to small business customers, the SBA is voluntarily notifying its business loan borrowers about this impending loan sale.

2.13 How are borrowers notified that their loans have been sold, and who to contact for information?

Prior to the servicing transfer the SBA will send a "Goodbye Letter" to each borrower. The letter will confirm that the borrower's loan has been sold, and provide information about the new servicer. The purchaser will also send a "Welcome Letter" to the borrower, directing them where to send their payment and who to contact for further information.

2.14 Can lenders purchase only their own loans in the sale (meaning those loans in which the lender owns a portion)?

No. Lenders who are qualified bidders may bid on any pool of loans, including a pool that contains the lender's loans. However, they must purchase the entire pool of loans, not just the portion of the pool comprised of their loans.

2.15 How will lenders know of future scheduled SBA loan sales?

The SBA retains financial advisors to promote market interest in each sale. Lenders and all potential bidders will be notified through advertisements and announcements in the media and trade publications. In addition, firms that are included on the SBA Investor Database will receive a direct marketing brochure. Finally, the date of each sale will be posted on the SBA Asset Sales website at <http://www.sba.gov/assets>.

To get on the SBA Investor Database, contact the Asset Sales Team at buyassets@sba.gov or send a letter to:

Small Business Administration
c/o Asset Sales Program
Attn: Margaret L. Hawley
409 Third Street, S. W., Suite 8300
Washington, DC 20416

3. THE LENDER CONSENT PROCESS

3.1 Which lender participated loans are scheduled for the sale?

Prior to each sale SBA will send lenders a Schedule of Assets included in the Lender Consent Package. Separate schedules for SBA-serviced and Lender-serviced loans are provided as attachments to the appropriate Consent Agreements. You also have the option, and are encouraged, to add additional loans to a sale that are not on the Schedule of Assets. However, loans with unpaid principal balances less than \$2,500 generally are not included in sale events unless they are part of a borrowing relationship, and another loan with the same borrower is also included in the sale.

3.2 Can a lender consent to sell only selected loans from the Schedule of Assets?

Yes. While the SBA would prefer to sell all of the SBA-purchased 7(a) and 502 loans, including loans serviced by the lender, a lender may consent to sell only selected loans.

If a lender supports the SBA's Asset Sales Program, but does not want to consent to sell all the loans on the Schedule of Assets, the lender should cross out those loans for which consent is not granted.

3.3 *Can a lender volunteer loans to asset sale events?*

The SBA plans to sell its direct loan and purchased guaranteed loan portfolio and its Development Company loan portfolio. Lenders are encouraged to contribute any Development Company loan or purchased guaranteed 7(a) loan with a total unpaid principal balance of more than \$2,500 in which they have a participated interest. Lenders may e-mail SBA at lenderquestion@sba.gov indicate their interest in volunteering loans for future sale events.

3.4 *How should a lender notify the SBA if it wants the sale to include its portion of the Section 7(a) loans that the SBA has identified for sale?*

The lender must send one or both of the signed agreements included in this Lender Consent Package, to the SBA to authorize sale of the entire loan, including the lender's portion. The lender should sign the appropriate agreements, either the SBA-Serviced Consent Agreement, the Lender Serviced Consent Agreement, or both agreements if applicable, and return them to the SBA as quickly as possible along with the corresponding Schedules of Assets.

3.5 *Can the lender sell loans in litigation?*

Loans in litigation can be sold at the discretion of the lender. However, once servicing has transferred to the purchaser, outside counsel should be terminated by the lender. Also, the lender cannot initiate new litigation without SBA's approval.

3.6 *How will a lender be notified when his/her loan is sold?*

Shortly after closing, SBA will send a letter notifying each lender which loans have been sold in Sale #5, and the reasons why any loans not sold were excluded.

4. PARTICIPATING LENDER COMPENSATION

4.1 *How much will lenders get paid for their portion of Section 7(a) and 502 loans that the SBA sells?*

In each loan sale, the loans are divided into loan pools in order to maximize value. The criteria used to pool the loans may include (but is not limited to): loan performance status, interest rate, maturity date, collateral type, lien position, loan to value ratios, location of collateral and environmental issues. The Transaction Financial Advisor will endeavor to stratify the loan portfolio into homogeneous pools to maximize the market value of the various loan assets.

Lenders will be paid their net pro-rata share of the proceeds from the loan pool(s) in which their loans were sold based on the following:

- (1) The unpaid principal balance of the loans in which the lender has an interest, expressed as a fraction of the total unpaid principal balance of the sold pool of loans, times
- (2) The total sales price of the sold pool of loans, less
- (3) The pro rata direct costs of that particular sale.

The SBA will cover the overhead costs associated with the Loan Sale Program. Lenders will not bear the costs of the Program Financial Advisor or the SBA staff. The SBA will deduct the direct

costs of each sale, including the costs of the Transaction Financial Advisor, outside legal, and due diligence contractor costs against the gross sale proceeds.

4.2 Can SBA provide an estimate of the expenses for Asset Sales?

The direct sale expenses on SBA Asset Sales have generally been 3% to 5% of the unpaid principal balance of the loans.

4.3 When will lenders get paid for their portion of Section 7(a) and 502 loans that the SBA sells?

There can be multiple successful bidders in a SBA asset sale. Closings will be scheduled as expeditiously as possible, generally within 30 to 60 days of the bid date. Servicing transfers will be scheduled within 15 to 45 days after closings. The SBA will remit the lender's share of the proceeds within 45 to 60 days of the last servicing transfer scheduled.

4.4 What is the procedure for remitting proceeds to lenders?

Proceeds checks will be issued by the U.S. Treasury. Concurrently, lenders will receive a letter from the SBA Finance Center that shows the loan number, UPB, borrower name, assigned bid price and net proceeds of each loan sold. In a limited number of instances, if the lender owes SBA monies that relate to the loans sold, the monies owed will be offset from the lender's sale proceeds.

5. SBA PROCESS FOR SELLING LENDER SERVICED LOANS

5.1 Does the SBA need a tape from the lender's servicing system? What about an updated Transcript of Account or other payment information?

The SBA will not be requesting servicing tapes from the lenders. However, it is critical that an updated, certified Transcript of Account, from the date of purchase by the SBA to the present time, be prepared and included in each servicing loan file.

A payment history that is produced by the lender's loan servicing system can be provided in lieu of the Transcript of Account. At a minimum, the payment history should include: the latest unpaid principal balance, the "as of date" and the interest paid through date.

The following statement should be included on all payment histories:

I certify that the above information is true and accurate.

Signed

Date

In the event there have been no transactions since the date of purchase by the SBA, the lender can certify the original Transcript of Account by adding the following statement:

I certify that the above information is true and accurate as of the date set forth below.

Signed

Date

Please be aware that the SBA balance and your balance must agree before the SBA can sell the loan. If your records indicate that the UPB on any of your loans differ from the SBA balance provided on the Schedule of Assets to the Consent Agreement, please attach any information you have that would assist in a reconciliation of the balances to your Transcript of Account.

5.2 *What information is needed from the lender's servicing and collateral loan files?*

The SBA provides comprehensive information to prospective bidders to maximize proceeds from the sale of loans and effectuate the transfer of servicing to the successful purchaser(s). The entire, original collateral and servicing loan files in the lender's possession must be provided to the SBA, including the original application, legal documents, appraisals, invoices for care and preservation of collateral ("CPC expenses"), remittance reports, borrower correspondence, Form 172 Reports on file, etc.

Electronic images of the collateral and servicing files will be available for bidders to review, and the original files will be provided to the successful purchaser(s) at closing.

5.3 *Are lenders required to provide the interest paid-to date?*

Yes. Lenders are requested to report the interest paid-to-date for each loan approved for sale on the Transcript of Account or payment history noted in Question 5.1.

5.4 *Is Form 172 reporting still required?*

Yes. Form 172 reporting will continue as usual until the servicing transfer date. Please comply with the SBA SOP, and provide remittances within 15 days of receipt.

5.5 *Will the SBA need updates to the loan files?*

Updates to the loan file, commonly referred to as "Trailing Documents", should be provided to SBA's Due Diligence Contractor on the first of each month. Please ensure that the SBA loan number is included prominently on the trailing documents. Trailing documents include borrower correspondence, such as compromise offers, bankruptcy filings or other legal actions, and invoices for property protection expenses, etc.

In addition to the existing Form 172 reporting, executed payoffs and compromises should be reported to your SBA Field Office contact as soon as they occur so the loans can be removed from the sale and the necessary documents returned to you. The SBA will pay to ship these documents. The shipment address is provided in Section 4.10.

5.6 *Must a post purchase review of a loan be completed prior to the sale of this loan?*

Yes.

5.7 *How should care and preservation of collateral ("CPC") expenses be handled?*

When a loan file is sent to the Due Diligence Facility, the lender should include the invoices for all prior and current CPC expenses that have **not** been reimbursed by the borrower. In addition, Lenders should submit expenses that have not been reimbursed by the SBA for payment as soon as possible, and continue to submit them to the SBA as incurred until the Closing Date. The Lenders should also send copies of all new invoices to the Due Diligence Facility as they are received.

5.8 *Is the lender required to sign the loan sale agreement or have any role or responsibility to close the transaction?*

No, both the SBA-serviced and Lender-serviced Consent Agreements provide the SBA with power of attorney that allows the SBA to execute the documents on the lender's behalf.

5.9 *Are there any special packing instructions for the loan file shipments?*

When preparing the loan files for shipment to the Due Diligence Facility, please adhere to the following instructions:

- 5.9.1 Prepare and include a Loan File Inventory Packing Sheet (Attachment VI) that lists the files that are shipped in each box. The Loan File Inventory Packing Sheet should clearly identify whether the files are collateral files only, servicing files only, or a combination of both files. In addition, please place the collateral and servicing files for a given loan in the same box.
- 5.9.2 If possible, all files for a given asset should be placed in one shipping box. If not, the box should be labeled 1A, 1B, 1C, etc. In addition, please number the boxes consecutively. Thus, only a single box will be labeled "Box #1".
- 5.9.3 Identify any parent notes, companion loans, and borrowing relationships on the Inventory Packing Sheet. If these loans are not listed on Schedule A, please include the loans on the appropriate schedule and ship the loans to the Due Diligence Facility.
- 5.9.4 Loans added to the sale by the Lender should be added to the Inventory Packing Sheet.
- 5.9.5 If possible, each loan file should indicate whether the file is (1) the servicing file; (2) the collateral file; or (3) the combined servicing and collateral file.
- 5.9.6 Display the SBA loan number prominently on the loan file and on the inventory sheet(s) included in the shipping boxes. The Lender's internal loan number should also be on the loan file.
- 5.9.7 Include a copy of the Lender Questionnaire, Attachment IV.

5.10 *Who will pay for the shipment of files? Where should files be shipped and when?*

Files are to be shipped via Federal Express 2-day delivery. The cost for the shipment of lender files can be billed to the SBA. The billing label is to be marked in the 'bill recipient' section and charged to Federal Express # 232404426. The file shipment address will be provided at a later date.

File shipment dates will be coordinated with your SBA Field Office contacts. The SBA will confirm expected shipment dates with the Due Diligence Contractor for lenders with greater than 20 loans who have requested Compact Disks (CD's) of the electronic images of their original files. This will ensure that lenders will be able to access the files needed to service their loans within 15 business days. Lenders who have not requested CD's do not need to coordinate shipment dates with the Field Offices.

5.11 *How will the lender continue to service the loans until servicing is transferred to the successful bidder(s)?*

If a lender has 20 or fewer loans in the sale, they must retain copies of the sections of the loan file that will be needed to service the loan(s) until servicing is transferred to the purchaser(s). If lenders have over 20 loans in the sale, they have the option of: (1) copying their own files or (2) requesting CD's with electronic images of their files. The SBA's Due Diligence Contractor will ship the CD's within 15 business days of receipt of the files. The electronic images of the files will have the collateral documents plus the most recent 5 years of correspondence in the servicing files.

All lenders should complete the attached questionnaire (Attachment IV) to provide contact information. In addition, if the lender has over 20 loans in the sale, indicate on the questionnaire whether a CD's is requested.

If original documents are required for unanticipated events, such as a loan payoff, lenders should notify SBA at lenderquestions@sba.gov. The required documents can be returned to lenders within 5 business days. If the lender needs a document that they did not copy, the SBA will provide a facsimile or copy within 48 hours.

5.12 *What servicing cut-off dates have been established?*

The servicing cut-off dates listed below are the last dates on which specific actions can occur on the loans being sold. It is required that all actions taken be in writing.

<u>Cut-off Date</u>	<u>Action</u>
3 months before bid date	Modification of the Terms of the Note
1 month before bid date	Collateral Releases/Subordinations and Collateral Substitutions; Deferments; Borrower Negotiations/Compromises, Third Party Sales and/or similar situations that extinguish the debt to SBA

There is no change in the manner in which loans with ongoing litigation will be handled during the sale. However, written consent from the SBA's office of General Counsel is required to initiate litigation.

Lenders should contact one of the following individuals by e-mail to request written consent:

William Gery, Counsel	E-mail: william.gery@sba.gov
Diane Jansson, Counsel	E-mail: diane.jansson@sba.gov

5.13 *What happens if a lender's unpaid principal balance does not agree with the SBA's balance?*

In some instances the SBA records may reflect a different unpaid principal balance from the balance reported in the lender's last Form 172 Report. As indicated previously, these principal balances will need to be reconciled by the SBA prior to the Bid Date. Lenders will be contacted in the event that the SBA has any questions about a reported balance.

5.14 *Will lenders continue to service the loans after the sale? How will the servicing transfer work?*

Lenders will continue to service the loans until the servicing transfer date, after which time, servicing will be transferred to the new purchasers. The servicing transfer date generally occurs approximately 60 days after the Bid Date.

The purchasers of the loans are entitled to 100% of all payments processed by the SBA after the Transaction Cut-Off Date, which is approximately three weeks before the Bid Date. Lenders must remit 100% of all payments received after the Transaction Cut-off Date to SBA, less any applicable service charge. Lenders will be instructed at a later date when to stop posting payments to the accounts, and other details on the servicing transfer.

Once the sales have closed, lenders will be notified which loans have sold and will be provided with the name, address and contact person at the new servicer. Trailing Documents should be sent directly to the new servicers after the closing date. Payments received after the servicing transfer date should be forwarded directly to the new servicer.

5.15 *Who will be responsible for notifying borrowers that their loans have been sold?*

On behalf of its lenders, it is anticipated that the SBA will send: (a) a notice to the borrowers to inform them of SBA's intent to sell their loan, and (b) a "Goodbye Letter" at the time of servicing transfer. The purchaser is responsible for sending a "Welcome Letter" to the borrower.

5.16 *What should lenders do about borrowers that continue to send payments after the servicing transfer date?*

Borrowers will be instructed in SBA's goodbye letter to send their payments to the new servicer after the servicing transfer date. They will also be asked to cancel any arrangement for automatic loan payments through electronic debits. SBA will provide the servicing transfer date to the lenders, and request that no payments received after that date be processed. Lenders will also be asked to contact the appropriate bank to discontinue the automatic loan payments, if the borrowers do not arrange for electronic payments to be stopped in a timely fashion.