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**NAGGL Gets TRAINING**

Michigan SBA Lenders Conference - Advanced Lenders Roundtable

Training & Events  
Advocacy  
Membership  
Industry Service

welcome :)

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**Quick Overview of Most Important Things  
Happening at – and to – SBA . . .**

- Transition at SBA
- Setting the Stage – Program volume
- Recovery Act Provisions and Implementation so far
- Thawing the Secondary Market
- Still Pending Legislative Request
- Other Happenings of Interest to Program Participants
- *Interim Final Rule* on Lender Oversight Program
- Last, but not least . . . SOP 50 10 5(A) changes

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**Current Issues**

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### Transition at SBA

- **New President . . . So what happens at SBA?**
- **After election – prior to inauguration**
  - Transition Team on board to pave way for new appointees and transition from old administration
  - Very early nomination of new SBA Administrator (December 19<sup>th</sup>) – but, confirmation still pending
- **After inauguration**
  - Senior career staffer named ‘Acting’ Administrator
    - Darryl Hairston
  - ‘Permanent’ political staff begins to come on board
  - Senate Confirmation of Administrator
  - Naming and confirmation of other senior leaders

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### Where Does SBA Stand Today?

- **Administrator Nominated – pending confirmation**
- **Chief of Staff on Board – Ana Ma**
- **Counselor to Administrator on Board – Ginger Lew**
- **AA/Capital Access appointed – Eric Zarnikow**
  - Appointed to position by President Bush (11/2007)
- **AA/Entrepreneurial Development appointed – Penny Pickett**
- **Other senior staff appointments, including Deputy Administrator, still to be made**

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### SBA Administrator Nominee Karen Gordon Mills

- **Most recent positions:** President of MMP Group, a private equity investor and adviser (Brunswick, ME); and, chair, Maine's *Council on Competitiveness and the Economy*
- **Quote:** "Building and growing a small business is a defining tradition in America. Many of us are the children of immigrants, men and women who are able to start and grow their own businesses. This is a legacy I'm proud to be a part of and to promote for our future." (December 19, 2009)  
[source: The Washington Post, December 20, 2008]

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## Current Program Volume

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## YTD Activity as of 2/28/2009

- 7(a) Volume is DOWN 57% in Numbers
- 7(a) Volume is DOWN 42% in \$\$\$\$
- Loans \$150k or less DOWN 62% / 58%
- Community Express DOWN 75% / 74%
- PLP loans account 62% of 7(a) \$\$\$\$
- Loans to startups account for 38% of 7(a) \$\$\$\$
- 504 Volume is DOWN 46% in Numbers
- 504 Volume is DOWN 45% in \$\$\$\$

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## SBA Portfolio Summary 7(a) Approval Statistics

7a Approval by Fiscal Year

Fiscal Year	Number of Loans Approved	Dollar Amount of Loans Approved (Millions)
1991	3.19	3.19
1992	5.81	5.81
1993	6.69	6.69
1994	8.14	8.14
1995	8.26	8.26
1996	7.7	7.7
1997	9.47	9.47
1998	10.6	10.6
1999	10.15	10.15
2000	10.52	10.52
2001	9.86	9.86
2002	12.27	12.27
2003	13.37	13.37
2004	15.22	15.22
2005	14.52	14.52
2006	14.26	14.26
2007	14.57	14.57
2008	12.57	12.57

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### Why is Loan Volume Down?

- Lack of Profitability in Program Participation
- Program Costs are UP
- Pricing Restrictions
- Weak Secondary Market
- Fewer 7(a) Lenders
- Fewer Borrowers
- Lesser-Quality Borrowers/Tighter Standards
- Lack of Liquidity in the Banking System

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### Membership Survey - November 2008 Reasons for 7(a) Volume Decline

- #1 - Decreased profitability of SBA lending due to lender fees and costs
- #2 - Inability to sell in secondary market
- #3 - Tightening of credit standards
- #4 - Borrower confidence waning
- #5 - Borrower demand down
- #6 - Declining Net Interest Margin (NIM)

• Top write-in suggestion – ALL fees too high

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### Membership Survey - November 2008

• Q: What steps need to be taken immediately to allow your institution to make more SBA 7(a) loans and serve more small business borrowers?

- #1 - Reduce or temporarily waive borrower & lender fees
- #2 - Increase maximum 7(a) loan size to \$3 million
- #3 - Government inject liquidity into secondary market so lenders can sell loans again
- #4 - Increase the maximum interest rate ceiling
- #5 - Implement alternative size standard
- #6 - Make other changes to secondary market

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**Recovery Act**

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**Recovery Act – 2/17/2009**

- \$375 Million for 7(a) and 504 Fee Relief
- \$255 million for *Bridge Loans* up to \$35,000
- Secondary Market financing
- 504 First Lien Loan Pools
- Temporary increase in maximum guaranty Percentage up to 90%
- Increased Surety Bond limits
- \$20 Million for technology systems to streamline SBA's lending and oversight processes
- \$25 Million for SBA staffing to meet demands of new programs
- \$10 Million for the Office of Inspector General

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**SBA Implementation**

- Policy Notice 5000-1097, "Implementation of Section 501 of the Recovery Act – Fee Elimination Provisions"
  - Effective 3/16/2009 – retroactive to 2/17/2009
- Policy Notice 5000-1098, "Implementation of Section 502 of the Recovery Act – Up to a 90 Percent Guaranty on 7(a) Loans"
  - Effective for loans processed on or after 3/16/2009
- Q & A
  - For SBA Participating Lenders
  - For Small Business Owners

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**SBA Policy Notice No. 5000-1097  
Fee Elimination Provision – 7(a)**

- Eliminates guaranty (borrower) fee
- Applies to all loans – retroactive to 2/17/2009
- Fees paid since 2/17 will be refunded by approx 5/1
  - Lender must refund to borrower
- Does not eliminate on-going fee
- Program level estimate – \$8.7 billion
- Duration of fee elimination – through approximately 12/31/2009

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**SBA Policy Notice No. 5000-1097  
Fee Elimination Provision – 504 Program**

- Eliminates two program fees:
  - Third-party Participation Fees
  - CDC Processing Fees
    - SBA will pay CDCs 2/3 of estimated fee at time of loan approval and balance immediately following debenture funding
- Retroactive to 2/17/2009
  - SBA will refund participation fees paid prior to Notice
  - SBA will reimburse CDC for fees paid prior to Notice
  - If borrower already paid fee – CDC must reimburse

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**Fee Elimination Provision – 504 Program**

- Program level estimate – \$3.6 billion
- Duration of fee elimination – through approximately 12/31/2009

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**Fee Elimination – Additional Guidance**

- **504 Fees**
  - CDCs specifically prohibited from canceling loans approved prior to 2/17 and resubmitting to qualify for reimbursement of processing fee
- **7(a) Fees**
  - Although not specifically prohibited by Notice, SBA has advised that the same policy applies to 7(a) loans approved prior to 2/17
    - Whether processed by same of different lenders

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**SBA Policy Notice No. 5000-1098  
Increased Guaranty up to 90%**

- Effective 3/16/2009
- Applies to all 7(a) loans except SBA Express
- BUT, maximum guaranty amount remains capped at \$1.5 million (aggregate)
- SO, 90% guaranty applies only to loans up to \$2 million
- For loans over \$1.6666 million guaranty calculated
  - \$1.5 mil divided by loan amount rounded down to 2<sup>nd</sup> decimal place

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**Policy Notice No. 5000-1096  
Additional Requirement**

- Recovery Act requires borrower to meet additional requirement for increased guaranty –
  - No loan guaranty may be made to any entity found by Secy of Homeland Security or Attorney General to have engaged in a pattern or practice of hiring, recruiting or referring for a fee, for employment in the U.S. an alien knowing the person is an unauthorized alien
- To comply, lender must require borrower or operating company to certify it has not been so found

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**Still to Come . . .**

- Implementation of \$35,000 'bridge' loan program
- What we [think we] know
  - \$255 million appropriation
  - Non-7(a) program
  - Eligibility = "Viable" businesses
  - Loans to be used to make loan payments on non-7(a) loans held by lender other than maker
- Likely implementation date – ????

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**Thawing the Secondary Market**

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**Term Asset Loan Fund (TALF)**

- Administered by FED and Treasury
- Source of Funds for Investors
- 2008 or 2009 Loan Pools
- 2008 or 2009 Loans
- Interest Rate – Fed Target + .75%
- Haircut
- Non-recourse Fee
- March 2009 Start
- ??Liquidity for the Secondary Market??

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### NEW INITIATIVE – Direct Purchase of Secondary Market Securities

- White House / Treasury announcement – 3/16/2009
- Treasury Department will purchase
  - Securities backed by 7(a) loans 'packaged' on or after 7/1/2008
  - New 7(a) securities 'packaged' between now and 12/31/2009 when the Emergency Economic Stabilization Act authority expires
  - First lien- mortgage securities connected to the 504 program 'packaged' on or after 7/1/2008
  - Securities issued from pooled 504 first mortgage loans under the new SBA secondary market guaranty program being developed by SBA under the Recovery Act

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### Direct Purchase of Secondary Market Securities

- Intent:
  - To "provide liquidity to lenders, including community banks and credit unions, enabling them to restart the process of recycling capital and extending loans"
- Complements TALF
  - Which is intended to provide investors with an attractive source of financing to keep existing secondary market in place "so that private investors can replace the government as the purchaser of these securities when market conditions return to normal"

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## Direct Purchase of Secondary Market Securities

- Projected Implementation Dates
  - 7(a) – by end of March
  - 504 – by May

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## What's Next?

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## Still Pending – NAGGL Legislative Request

- Increase Maximum Loan Size to \$3 million
- Increase Maximum Guarantee to \$2.25 million
- Use of the Alternate Size Standard in 7(a)
- Combination of Maximum Guarantees - 7(a) + 504
- Rate Basis Other Than Prime/LIBOR (10-Year CMT)
- Suspension of Lender Oversight Fees

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**Other Items**

- **FY 2010 Budget – Hearings in April**
- **GAO Report on *Credit Elsewhere* – released 3/16/2009**
- **GAO Review of Lender Oversight – expected completion fall 2009**
- **GAO Review of 7(a) Secondary Market**
- **GAO and IG Reviews of Recovery Act implementation**

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**Meanwhile Back in the Program . . .**

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**Another Very Busy Year for SBA**

- **Issuance of SOP 50 10 5 and revised SOP 50 10 5(A)**
- **Rewrite of SOP 50 51 underway**
- **Introduction of Small/Rural Lender Advantage**
- **Re-introduction of Community Express**
- **Continuing efforts to streamline guaranty purchase process**
- ***Interim Final Rule* on Lender Oversight**

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### Interim Final Rule – Lender Oversight Program

- **Published:** December 11, 2008
- **Effective:** January 12, 2009
- **Interim Final** – means that even though Rule has taken effect, SBA is seeking additional comments
- **Comment period closed:** March 11, 2009
- **SBA will review comments and may OR may not make changes to Rule**

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### Background

- **Rule covers:**
  - **7(a) Lenders**
    - Small Business Lending Companies
    - Non-Federally Regulated Lenders
    - Regular 7(a) Lenders
  - CDCs
  - Microloan Intermediaries and Non-lending Technical Assistance Providers
- **Authority derived from various oversight/regulation provisions of Small Business and Small Business Investment Acts**

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### Major Provisions of Rule

- **Incorporated SBA's risk-based lender program and established responsibilities of OCRM in the business loan program regulations, including:**
  - Accounting and Reporting Requirements
  - Offsite Reviews/Monitoring
  - Onsite Reviews/Examinations
  - Capital Adequacy Requirements
- **Established the types of, grounds for, and procedures governing SBA enforcement actions**

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## Heavy Reliance on Risk Rating System

- For NAGGL – Single **BIGGEST** concern
- Requested implementation be deferred until 3<sup>rd</sup> party validation completed
  - Such validation now underway at Government Accountability Office

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## Agency Response

- **NO** change to proposed
  - Risk Rating System is “a reasonable internal tool for assessing portfolio risk . . .”
    - Developed with D&B and Fair Issac and annually validated by them since 2004
  - But, noted that system
    - Will be used “in combination with other factors when evaluating satisfactory SBA performance”
    - NOT expected to be sole basis for taking enforcement actions
    - Can be adjusted based on changes in economic situation

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## SOP 50 10 5(A) Revisions

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**SOP 50 10 (5)(A) Revisions**

- **SOP 50 10 5 took effect: August 1, 2008**
- **SBA Notice # 5000-1092, effective February 6, 2009 announced 1<sup>st</sup> revision**
- **Changes took effect March 1, 2009**
  - **As amended by information Notice # 5000-1096**
- **Notices and various versions of revised SOP available at [www.sba.gov/banking](http://www.sba.gov/banking)**

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**SOP 50 10 (5)(A) Revisions**

- **Changes outlined in notice include:**
  - **Incorporation of all policy and procedural notices between 1/1/2008 and 12/31/2009**
  - **Small/Rural Lender Advantage changes (from Notices 5000-1045 and 5000-1056)**
  - **CommunityExpress changes (from Notice 5000-1068)**
  - **New LIBOR + 300 basis points base rate and modification of guidance on selecting initial not rate (from Notices 5000-1081 and 5000-1082) . . .**

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**More . . .**

- **New guidance on financing goodwill**
- **Clarified guidance on working capital documentation**
- **Modified guidance on environmental provisions and appendices**
- **Modified guidance on post-construction certification requirement**
- **Clarification of 'no adverse change' findings requirements for CDCs**
- **Update regulation references to incorporate Interim Final Rule on Lender Oversight Program**

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### Lender Categorization

- Revises definition of “Federally Regulated Lenders” to list federal regulators
  - Federal Deposit Insurance Corporation
  - Federal Reserve Board
  - Office of the Comptroller of the Currency
  - Office of Thrift Supervision
  - National Credit Union Administration
  - Farm Credit Administration
- Revises definition of “SBA Supervised Lenders” to exclude reference to Farm Credit Administration system lenders

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### Preferences

- Specifies that lenders must ‘be particularly careful’ to avoid establishing a preference when using its delegated authority (for example, reducing its existing exposure to the borrower through the use of an SBA guaranteed loan)

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### Lender Oversight

- Adopts the requirements of the *Interim Final Rule on Lender Oversight* which took effect January 12, 2009

[Comment period closed March 11, 2009]

Pages 14-17 and throughout

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## Community Express Pilot Program

- **Adopts the requirements of Notice # 5000-1068, effective September 16, 2008**

Pages 46-48, 118-131 and throughout

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## Small/Rural Lender Advantage Initiative

- **Adopts the requirements of Notice #s 5000-1056 and 5000-1060, effective May 12, 2008 and June 26, 2008, respectively**

Pages 79-80, 171-174 and throughout

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## Eligibility – Size

- **Adds definition of ‘affiliation’ from SBA size regulations:**
  - “Affiliation exists when 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, previous relationships with or ties to another entity, and contractual relationships when determining whether affiliation exists”
- **Clarifies that when an existing business is acquiring another business, the combined size is used to determine eligibility**

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### Eligibility – Franchise

- Expands explanation of assistance through franchise.gov: “information with respect to a specific franchise, to find out if SBA counsel have determined an agreement is unacceptable and to request statistical information” [Formerly said “for information about franchise eligibility reviews.”]
- Explains that mailbox not designed to evaluate franchise material
  - Advises lenders to contact SBA district counsel or SBA Franchise Counsel “for specific questions regarding eligibility determinations”

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### Franchise Eligibility If Listed on Registry

- Adds requirement: If footnote requires an addendum, lender must obtain executed addendum to show compliance
- Deletes requirement that file include proof of FTC Registration
- If material change:
  - Requires certification to be forwarded to SBA Franchise Counsel [formerly loan processing center]
  - States that the agreement and all related documents are required as if not listed on the Registry

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### Franchise Eligibility Not on Registry

- Amends language to state that if agreement previously determined to be unacceptable, with no fix negotiated and offending provisions still in place, applicant “may still be ineligible”
  - Previously said “applicant is ineligible”

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### Franchise Eligibility Gas Stations

- Adds additional requirements regarding gas station eligibility
- Previously incorporated by reference to Appendix 5

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### Eligibility – Passive Businesses

- Restores SOP 50 10 (4) eligibility standard for hotels, motels, trailer (i.e., RV parks), campgrounds, or similar businesses
- Eligible if more than 50% of prior year's revenues derived from transients who stay for 30 days or less at a time

[Standard for mini-warehouses/office suites/shopping centers/flea markets/mobile home parks is unchanged = more than 50% of prior year's revenues from services rather than rental income]

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### Passive Businesses Documentation

- Adopts information in FAQ regarding required documentation
- Applicant must break down revenue into passive (rental) and service if startup incomes
  - must breakdown projections
- Eligible if more than 50% of prior year's revenues (or projections) derive from services
- If applicant does not bill separately for services and majority of revenue is passive – applicant must show that expenses associated with providing services is more than 50% of total revenue

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**Eligibility – 912 Processing**

- Clarifies that for SBA Express and Patriot Express processing when lender cannot clear application
  - Lender **must** send Form 912 and any supporting documentation to the local field office
- Makes other 'nuanced' changes to further clarify 912 processing requirements for all loans

Pages 101-108

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**Debt Refinancing**

Amends list of credit terms eligible for refinancing -- new list:

- Long term debt with demand note or balloon payment
- Debt with an interest rate that exceeds SBA maximum for processing method being used
- Credit card debt
- Debt that is overcollateralized based on SBA's requirements . . .

Pages 132-134

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**Debt Refinancing (cont)**

- Revolving LOCs (short or long term) where original lender is unwilling to renew line or applicant is restructuring its financing for longer term or lower rate
- Debt with a maturity not appropriate of the financing purpose
- Debt not identified above but Lender believes no longer meets needs of applicant [Requires regular 7(a) processing]

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### What Do Changes Mean?

- Provides much more clear guidance regarding when refinancing is permitted
- Appears to allow refinancing of debts – particularly lines of credit – that had not been deemed eligible under recent interpretations
- **NOTE:** no change to 20% cash flow improvement for long-term debts

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### Use of Proceeds for Relocation

- Restores as an ineligible use of loan proceeds – financing the relocation of a business out of a community if there will be a net reduction of 1/3 of its jobs or a substantial increase in unemployment in any area of the country
- Provides exception if:
  - Relocation is for key economic reasons and crucial to continued existence, well-being, etc.
  - AND**
  - Economic development benefits to applicant and receiving community outweigh negative impact on losing community

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### Rentable Space

- Clarifies that when there will be residential space rented to a 3rd party, must conform to regular lease-out limitation
  - For new construction – no more than 20% permanently leased out and an additional 20% for a period not to exceed 10 years
  - For purchase of existing building – no more than 49% permanently leased out

Pages 137-138

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### Financing Goodwill

- Adds a cap to the amount of loan proceeds that may be used for purchase of goodwill
  - 50% of the loan amount up to a maximum of \$250,000
  - Loan Authorization must reflect goodwill as a separate use of proceeds

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**BUT . . .**

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### Temporary Change to Goodwill Financing Policy

- SOP policy amended by Information Notice No. 5000-1096, effective 2/27/2009, (policy expires 8/31/2009)
  - Allows loans where goodwill exceeds SOP limits to be submitted for standard (non PLP) processing
  - In asset purchase
    - goodwill = selling price – sum of the book value of all assets being purchased
  - In stock purchase
    - Goodwill = selling price – (the sum of the book value of all assets being purchased minus the sum of all liabilities that are being assumed)

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### Alternate Process

- Without data, in response to comments regarding limited options – SBA allowing lenders to submit applications that do not meet the 50 10 5(A) requirements though the Standard 7a Guaranty Processing Center for SBA consideration
- Alternate process to be in place through August 1, 2009
- During this period SBA will collect info from applications and analyze types of businesses and transaction structures submitted

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### NAGGL Survey

- NAGGL will be issuing a formal survey asking lenders to provide historical data on goodwill financings
  - Data broken down by business industry –
    - How many approved applications would not fit new limitation?
    - How are loans with more than \$250.0 in goodwill performing when compared to other loans?
- NAGGL also requests that members notify NAGGL of outcomes of loans processed through LGPC –
  - Approvals? Declines?

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### Business Valuations

- Requires outside valuation if amount being financed (from all sources) is more than \$250,000 (down from \$350,000) or if close relationship between buyer and seller BUT
- Now excludes from that amount appraised value of real estate and/or equipment

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### Maximum Maturity – Working Capital and Intangibles

- Allows a maximum maturity for working capital and the purchase of intangibles to be 10 years
- Deletes requirement for additional justification if term exceeds 7 years

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### Maximum Maturity – Refinancing Business Assets or a Business Acquisition

- Refinancing real estate or fixed assets – remaining useful life of the assets
  - Documentation required
- Refinancing business acquisition – 10 years UNLESS
  - Largest percentage of small business' assets is real estate, THEN 25 years

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### Interest Rate Changes

- Per Notice #s 5000-1081 and 5000-1082
  - Adds LIBOR to acceptable base rates
  - Specifies that date for determining base rate now the 1st business day of the month in which the loan is made
  - Allows loans priced using SBA Peg Rate to be sold in secondary market

Pages 150-152

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### Lender Service Provider Services

- Deletes prohibition against 'underwriting' as a service under a Lender Service Provider Agreement
- Appears lender can now contract for underwriting services
  - However, lender remains fully responsible for all loan decisions – LSP only assists

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### Definition of Substantial Renovation

- Adopts CAPLines definition for “substantial renovation”
  - Rehabilitation expenses = more than 1/3 of the purchase price or fair market value at the time of application

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### Construction/Substantial Renovation Appraisals

- Removes requirement that the appraiser ‘certify’ that construction completed according to plans and specs, etc.
- New requirement: Lender must obtain a ‘statement’ regarding “as-completed” value
- If value is less than 90% of original estimate, appraiser must state reason for change, e.g., changes in market conditions or deviations from original plans

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### Documenting Disbursement for Working Capital

- If Authorization identifies working capital for normal operating expenses (e.g., payroll, utilities, etc) as a use of proceeds
  - W/C disbursement does not need to be documented

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**Environmental Changes**  
To be covered in a separate session

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**SBA Still Seeking Feedback**

- Send questions, comments, suggestions for SOP improvement to SBA's SOP mail box: [SOP50-10Modernization@sba.gov](mailto:SOP50-10Modernization@sba.gov) – and please copy [info@naggl.org](mailto:info@naggl.org)
- SBA is not providing individual answers through that mailbox, but will consider information provided as they complete technical corrections of this edition, and consider changes for future updates

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**And, Don't Forget . . .**

- **SBA SOP Clarifications – FAQs**  
[Available at [www.sba.gov/banking](http://www.sba.gov/banking)]  
- General  
- Environmental
- Expect more to come – including, hopefully additional information on goodwill
- **AND, PLEASE . . .**  
- Respond to NAGGL survey on business acquisition transactions **AND**  
- On an on-going basis, send information regarding approvals/declines of business acquisition submitted to LGPC

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**We're Finished!**

- Thank You!

- Contact Information:  
[info@naggl.org](mailto:info@naggl.org)

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