

CHAPTER 6 - GUARANTY PURCHASES

SOP 50 51 2A, Ch. 13

REQUESTING THAT SBA HONOR ITS GUARANTY

SBA reviews a lender's request that SBA honor (purchase) the guaranty to determine whether the lender has complied with SBA loan requirements and prudent lending standards so that payment of the guaranty is appropriate. The amount and types of documentation that lender must include in its guaranty purchase package depends on the type of loan, use of proceeds, collateral, and other factors. SBA conducts its review prior to purchasing its guaranty when SBA purchases directly from the lender ("pre-purchase review"), and conducts its review after purchasing its guaranty when SBA purchases directly from the secondary market holder ("post-purchase review"). SBA rarely purchases without a lender demand, but it has regulatory authority to do so in its sole discretion (13 C.F.R. § 120.520).

SBA PURCHASE REQUIREMENTS

In addition to any agreements a lender has signed with SBA, the following are sources of information on SBA requirements for purchases:

- Regulations: 13 C.F.R. §§ 120.120 - 120.124.
- Standard Operating Procedures (SOPs):
 - SOP 50 50 4A, Ch. 9 and 10;
 - SOP 50 51 2A, Ch. 13;
 - SOP 50 50 4A Ch. 6, para. 6.c (LowDoc loans);
 - SOP 50 50 4A Ch. 6, para. 9.f (Export Working Capital Program (EWCP) Loans).
- Notices General:
 - Procedural Notice 5000-898 (Dec. 2003);
 - Policy Notice 5000-831 (October 2002)
- Notices on *SBAExpress*:
 - Information Notice 5000-819 (Sept. 2002);
 - Procedural Notices 5000-813 (July, 2002); 5000-803 (June 2002)
- Forms: Guaranty Purchase Checklist (Appendix 6-B)
- Program Guides: *SBAExpress* Program Guide, Sections (Secs.) 8 and 9.

TIME TO REQUEST PURCHASE

A lender first may request payment on the SBA guaranty for loans made under most SBA loan programs following a 60-day uncured delinquency. However, in all loan programs SBA strongly encourages lenders to fully liquidate the loan prior to requesting purchase.

Special rules for certain loan programs:

- LowDoc Loans (SOP 50 50 4A Ch. 6, Para. 6.c.)
 - A Lender can request purchase when:
 - Lender has liquidated all personal property, except in bankruptcy situations, and
 - Lender has indicated in writing how it will pursue all other sources of recovery.
 - SBA will pay a maximum of 120 days of accrued interest.
 - SBA will share in the reasonable and necessary expenses on a pro-rata basis up to its share of total recoveries.

- SBAExpress loans (SBAExpress Program Guide, Sec. 8)
 - Lender can request purchase when it has fully liquidated all collateral and pursued all avenues of collection. Exceptions:
 - SBA will immediately process the purchase request of all Export Express Loans; and
 - SBA will immediately process the purchase request of any SBAExpress loan that:
 - Has a principal balance of \$50,000 or less at the time of the purchase request, or
 - Involves, regardless of the loan balance, bankruptcy, judicial foreclosure, litigation or other unusual liquidation circumstances likely to extend the liquidation process more than 90 days past the earliest date that the lender could request purchase. (Generally, the earliest date a lender could request SBA to purchase is when there has been an uncured default exceeding 60 days.)
 - When requesting the purchase of an SBAExpress loan with a balance of \$50,000 or less, the lender generally will not be required to substantiate the liquidation of business assets, although the lender must document the liquidation of all business assets in its wrap-up report.
 - SBA will pay up to 120 days of interest.

- EWCP (SOP 50 50 4A, Ch. 6, Para. 9.f). Lenders may make demand as soon as the loan is classified as being in liquidation and 30 days after the earliest uncured payment default, but must not make demand later than 120 days after the earliest uncured payment default (See also SOP 50 51 2A, Ch. 10, Para 3).

HOW AND WHERE TO REQUEST PURCHASE

SBA encourages lenders to submit purchase documentation in a uniform and organized fashion, which may also result in a faster processing time by SBA. SBA recommends that lenders use the Guaranty Purchase Checklist, and place documents in the purchase package in the same order as they are listed in the Checklist (each document is assigned a number on the Checklist, in the left-hand column), with corresponding numeric tabs or hand-written numbers on the front of the document, lower right-hand corner.

Purchase requests, along with all documents required for processing, should be submitted to the office that currently oversees servicing of the loan. If the loan is in regular servicing status in either the SBA Fresno or Little Rock Commercial Loan Service Center, send your request directly to the appropriate center, and the loan file and your purchase request will be sent by that office to the National Guaranty Purchase Center located in Herndon, Virginia. If your loan is in liquidation status and already assigned to the Herndon center, send your guaranty purchase request directly to Herndon and your request will be matched with the loan file and assigned to a loan officer.

Addresses for the Commercial Loan Servicing Centers:

SBA CLSC East
2120 Riverfront Dr., Ste 100
Little Rock, AR 72202

SBA CLSC West
2719 N. Air Fresno Dr., Ste 107
Fresno, CA 93727

(501) 324-5871, x303

(559) 487 – 5650

Address for the National Guaranty Purchase Center:

SBA National Guaranty Purchase Center
1145 Herndon Parkway, Ste. 900
Herndon, VA 20170

(703) 487-9283

- The address to access the purchase center's web page is <http://www.sba.gov/banking/herndon.html> .
- You may e-mail the center at sbapurchase@sba.gov for issues relating to guaranty purchases, or loanresolution@sba.gov for general liquidation issues.
- Questions or concerns may also be faxed to 202-481-4674.

DOCUMENTATION REQUIRED FOR PURCHASE

Streamlined and Standard Purchases: SBA has two types of purchase procedures, depending on the size of the loan balance remaining at the time of lender's purchase request and other factors: streamlined purchase procedures and standard purchase procedures. In all cases, a Lender must submit, at a minimum the following documents (see Guaranty Purchase Checklist):

- (1) Written demand that SBA purchase the guaranty, including,
 - Date of default
 - Interest-paid-to date
 - Interest rate at time of default (see discussion in Standard Purchase Procedures regarding reimbursable interest)
 - Next installment due date
- (2) Wire transfer instructions

- (3) Certified transcript of account (SBA Form 1149 or lender's equivalent) signed by the lender (see discussion below for details)
- (4) Copy of signed Authorization and amendments
- (5) Copy of signed Note (must be on SBA Form 147 except SBA*Express* loans)
- (6) Copy of signed Guaranties (if required by the Authorization) (SBA Form 148)
- (7) Risk management database information
- (8) If the lender has completed liquidation on the account, the lender also must submit:
 - Lender certification that liquidation is complete and that all avenues of recovery have been exhausted
 - Final liquidation wrap-up report
- (9) For LowDoc and PLP Loans, documentation relating to the lender's eligibility determination (see discussion below)

Lender Transcript of Account: SBA requires lenders to submit for all guaranty purchases a Transcript of Account (SBA Form 1149 or lender's equivalent). Directions for completion of SBA Form 1149 are located on SBA's website at www.sba.gov/library/forms.html. While lenders have a variety of automated reporting and tracking systems and so may provide their own transcript as an alternative to the SBA Form 1149, the transcript of account **must** contain these elements:

- SBA loan name and 10 digit loan number.
- Method used for interest computation (360 day or 365 day).
- Date and amount of each disbursement.
- Date and amount of each payment showing principal and interest applications.
- Date to which interest is paid (which should be the same date payment was received).
- Interest rate changes (for variable rate loans).
- Next payment due date (defined as the "default date," at which point the interest rate becomes fixed; no changes to the rate should be reflected thereafter).
- If applicable, amount of Lender's successful bid at foreclosure sale (reflected on the transcript as a credit to the principal balance).

If lender uses its own form of transcript of account, lender must provide the following certification:

"I certify this to be a true copy of transcript of account."

Name

Date

Title

Lender Name

Loan eligibility documentation for PLP-processed and LowDoc loans: For all purchases involving loans processed as PLP, SBAExpress or LowDoc, SBA will review the eligibility of the loan for SBA-guaranteed financing, because SBA does not perform an independent review of eligibility at the time of loan approval. Lender must provide a copy of the eligibility checklist and supporting documentation lender used in its eligibility determination. If a PLP, SBAExpress or LowDoc loan is found to be ineligible, SBA will request that the lender voluntarily release the guaranty (or repay SBA if SBA purchased the loan from the secondary market). Note: a completed eligibility checklist alone will not be sufficient in confirming that the loan was eligible.

Streamlined Purchase: SBA will follow a streamlined purchase procedure, and generally not request additional documentation from the lender, if the following three criteria are met:

- (1) The SBA share of the outstanding principal loan balance is \$10,000 or less; and,
- (2) The loan did **not** experience early default/early loan problems (see below); and,
- (3) There is **no** suspicion of fraud or misrepresentation and **no** indication of a conflict of interest on the part of the borrower or lender.

Early default or early loan problems: SBA will not purchase early default or early loan problem loans using the streamlined purchase procedure. “Early default” means that a default in payment or business failure has occurred either prior to final disbursement of the loan, or within 18 months from the date of final disbursement. A default includes an unremedied failure to make one or more loan payments in accordance with the terms of the Note, as well as events that would place a loan in liquidation (see SOP 50 51 2A, Chapter 4, Paragraph 6). “Early loan problems” arise when either prior to final disbursement or within the first 18 months after final disbursement, a borrower consistently makes late payment (over 60 days late) or partial payments, or funds monthly payments through the sale of collateral, or the lender has deferred two or more consecutive scheduled payments. SBA reviews early default or early loan problem loans with a very high degree of scrutiny, and determines whether any deficiency by the lender in making, servicing, or closing the loan contributed to, or allowed, the early default or early loan problems. For all guaranty purchase reviews involving a PLP-processed loan that has gone into early default or experienced early loan problems, the lender must submit complete copies of its credit memorandum, supporting documentation relied on in its credit analysis, the borrower's application for the loan, and SBA Form 912 (Statement of Personal History) for each principal.

Additional documentation required for standard purchase procedures: If a loan is not eligible for streamlined processing, SBA will notify the lender as to which additional documents it will need for its purchase review by checking the appropriate boxes on the Guaranty Purchase Checklist. However, lenders may be able to expedite SBA’s review through providing the following documents in its initial purchase package, as applicable given the terms of the loan.

- **Site visit report:** Lenders must perform site visits within specified timeframes and prepare a comprehensive and detailed report containing an inventory of assets

and an assessment of their condition (see SOP 50 51 2A, Chapter 8, para. 8). Lender must include such site visit reports in its purchase package. If the site visit report indicates that collateral valued at more than \$5,000 was missing at time of the site visit, a referral to SBA's Office of the Inspector General (IG) is mandatory. A copy of the lender's IG referral should be included in the purchase package. Refer to SOP 50-51-2A, Chapter 24, para. 7.a.(2).

- **Bankruptcy:** If a bankruptcy has been filed and lender has not previously notified SBA, the purchase package should include the bankruptcy schedules, notices, other court filings, and proof of claim filed by the lender. If lender does not submit this information, SBA may not process the purchase request, depending on the type of bankruptcy filing and the date of the filing, because the information may have a significant impact on the determination of SBA's obligation to honor its guaranty.
- **Use of proceeds:** The lender must submit documentation that shows the lender disbursed the loan proceeds in accordance with the Authorization. With the exception of SBA*Express* loans, the lender must submit copies of the Settlement Sheet (SBA Form 1050) used in disbursing the loan.
- **Deeds of trust/mortgages:** If the Authorization requires real estate collateral to secure the note or a personal guaranty, the lender must include a copy of the deed of trust/mortgage in its purchase package. SBA reviews the deed of trust or mortgage to determine whether it was properly executed and recorded.
- **Title policy:** When real estate is required as collateral, the Authorization generally requires a title policy or report. If required, a copy must be provided in lender's purchase package.
- **Guaranty (SBA Form 148):** Holders of a 20% or more ownership interest in the small business generally must guarantee the loan. SBA Form 148 is a mandatory form and lenders cannot substitute their own form (this also applies to SBA Form 148L, Limited Guaranty).
- **Appraisals:** If an appraisal was required in the Authorization or by SBA policy, lenders are required to submit, at a minimum, the summary section from the beginning of the appraisal that indicates the appraised value and the date of valuation. However, SBA may request a copy of the full appraisal.
- **Environmental issues:** The environmental requirements for processing 7(a) and 504 loans are set forth in Chapter 1 of this Guide. The Authorization will state if any environmental reports were required. If so, the lender must submit, at a minimum, the summary and recommendation pages from any environmental report obtained, or if no report was obtained, an explanation for this omission with citation to the relevant provisions in SOP 50 10 4E.

- **Business asset collateral:**
 - **Security agreement:** If the Authorization required business personal property collateral, the lender must submit a copy of the security agreement with its purchase package. SBA reviews the agreement to determine whether it was properly executed by the appropriate individual or entity.
 - **UCC financing statements and renewals:** Lender must submit evidence of UCC lien filings and renewals, along with necessary lien searches. SBA will determine whether Lender properly perfected its lien and obtained the lien position required by the Authorization. If Lender has sold the collateral, SBA will review the recovery and expenses to assure that the Lender properly handled the liquidation and maximized recovery consistent with its lien position. If Lender did not obtain the proper lien position, SBA will analyze the amount of loss to SBA, if any, resulting from the improper lien position. If lender obtained a lien on the required collateral but did not include a lien search in its purchase package, SBA may proceed with the purchase but notify the lender that SBA will review liquidation of the remaining collateral later, to determine if there was any material loss to SBA if the lender failed to obtain the required lien position.

- **Life insurance:** If the Authorization required life insurance on a principal of the borrower or guarantor, SBA may require documentation pertaining to proper assignments and the continuation of coverage.

- **Flood insurance:** If required by the Authorization, lender should provide either: (a) certification that collateral is not located in designated flood area, or (b) evidence of flood insurance coverage.

- **Hazard insurance:** Lender must submit evidence of hazard insurance coverage and a lender's loss payable clause (for personal property collateral) or mortgagee clause (for real property collateral). If a policy has lapsed, lender should submit copies of the letters sent to borrower and all guarantors notifying them of lapse of coverage and requesting reinstatement.

- **Borrower injection:** If the Authorization requires borrower injection (usually in the form of cash or assets), lender must obtain evidence that the injection was made *prior to first disbursement*.
 - **Cash injection:** The Authorization will state the amount of the required cash injection, and usually the intended use. Satisfactory evidence for a cash injection generally consists of copies of processed checks, bank account statements (showing the borrower's account balances before and after the injection) dated prior to but near loan disbursement, or a signed and dated escrow settlement statement along with a bank statement

showing the injection into the business. Lender must submit credible evidence that the borrower did not use the disbursed loan proceeds to fulfill the cash injection requirement. If a cash equity injection is material to the borrower's operation, the lender must verify and document the existence of the cash injection so that it can reasonably be presumed that the funds will be used for business purposes.

- **Injection using borrowed funds:** The Authorization will set forth the documentation required; generally, there must be a full standby agreement (SBA Form 155 or comparable) providing that the loan for cash injection will not be repaid until the SBA loan is fully paid. If a standby is required, lender should submit a copy of the standby agreement and a copy of the debt instrument. If the lender makes a loan to an individual for purposes of a cash injection (or is aware of a loan made for this purpose), the lender must provide a full standby agreement or demonstrate that the loan can be repaid from a source other than the borrower business, or from reasonable withdrawals of salary from the business.
- **Asset injection:** The Authorization will specify the valuation requirements; appraisals may be required. The dollar amount of assets to be injected is based on the fair market value of the assets at loan inception. SOP 50 10 4, subpart A, chapter 4, paragraph 1(f) (4) requires lenders to carefully determine the value of non-cash assets injected into the business.
- **IRS tax verification:** On loans approved after October 7, 1994, SBA requires IRS tax verification transcripts to be obtained from the IRS using Form 4506, except for start-up businesses. These must be part of the purchase package for all early default/early loan problem loans, and may be required on loans that go into default later if necessary for the purchase review. The IRS verification policy applies regardless of whether it is specifically mentioned in the loan authorization.

Borrower resolutions deleted

- **Collateral lists:** Some Authorizations require that the lender obtain a listing of collateral prior to closing the loan, complete with a description and serial number of the items. The lender should provide a copy of the list with the purchase package.
- **Liquidation and Litigations Plans:** If the lender is requesting purchase prior to conducting liquidation and debt-collection litigation, these plans may need to be included with the purchase request if not already submitted to SBA.

PAYMENT OF INTEREST

(1) If SBA receives a lender's complete purchase package within 120 days of default, then all interest is payable to the date of the purchase payment, including interest during

the time SBA is processing the purchase, and also from the interest-paid-to-date until the date of default.

(2) If SBA does not receive lender's complete purchase package within 120 days from the date of default, only 120 days of interest is payable.

(3) If lender has liquidated the loan prior to requesting purchase, lender is allowed to recover up to 120 days of accrued interest from liquidation proceeds.

The rate of interest is the rate in effect on the day that the loan went into default. These interest days should begin with the interest-paid-to date up to 120 days maximum. SBA will then purchase the guaranteed principal balance remaining. Late charges are not covered under SBA's guaranty agreement with a lender and therefore lender cannot recover such fees from liquidation proceeds.

Due to legislative changes, for loans that were approved between September 28, 1996 and September 30, 2000, SBA will pay the lender the rate of interest indicated in 13 C.F.R. § 120.122 less one percent. SOP 50 50 4A, Ch. 9, Para. 8.b. Congress eliminated this requirement for loans approved after September 30, 2000. See SBA Procedural Notice 5000-703 (Dec. 2000).

Lender also should refer to the discussion below of the payment of interest for guaranties that are sold in the Secondary Market and 13 C.F.R. §§ 120.521, 120.522, and SOP 50 50 4A, Ch. 9, Paras.7-8.

PURCHASE FROM THE SECONDARY MARKET

SBA strongly encourages lenders to purchase directly from the secondary market holder those defaulted loans that lenders had sold in the secondary market after loan closing and disbursement. If the lender will not purchase, it must notify SBA in writing, and SBA will immediately purchase the loan and then perform a post-purchase review. If the lender purchases from the secondary market, and subsequently requests an SBA purchase, SBA will perform a standard pre-purchase review.

Documentation for secondary market purchase by SBA

- **Written notice and request for transcripts:** The lender must advise SBA **in writing** that it will not purchase from the secondary market. SBA will then notify both Colson Services Corp. and the lender that SBA will purchase the guaranteed portion. The lender must send any future loan collections to SBA's Denver Finance Center using SBA Form 172.
- **Complete and certified lender's transcript of account:** Within 5 business days of receiving SBA's notice of intent to purchase from the secondary market, the lender must submit to SBA a complete and certified transcript of account. SBA will reconcile the transcripts provided by Colson and the lender. SBA may request the

lender's assistance in the reconciliation process. If a lender's transcript is not received timely, or if SBA cannot complete reconciliation, SBA will use the Colson transcript and proceed with the secondary market purchase.

- **Payment of accrued interest:** SBA must purchase all accrued interest from the interest-paid-to date up to the date of guaranty purchase from the secondary market holder. If there was a delay in purchase caused by the lender, SBA will bill the lender for the excess interest purchased.
- **Post-purchase review:** SBA will conduct a post-purchase review to determine the appropriateness of the guaranty payment. In order to expedite the post-purchase review and minimize documentation requests, SBA recommends that lenders submit a complete guaranty purchase package to SBA using the procedures outlined above for standard purchase reviews. Lender should submit the package either concurrently with the written demand for purchase or shortly thereafter. If a lender fails to provide necessary documentation requested by SBA within 30 calendar days of the request, and fails to provide a satisfactory written explanation as to why it cannot provide the requested information, SBA may consider this to be a material failure to comply with SBA loan requirements and can serve as a basis for SBA to seek recovery from the lender of the amount paid to the secondary market under the guaranty. Similarly, missing documentation can support a partial recovery to the extent that the documentation in question relates to specified collateral or other loan requirements.

DENIALS OF LIABILITY AND “REPAIRS”

SBA's general policy for guaranty purchases is to reach a fair decision based on a thorough review of lender's purchase request and all relevant documentation. If a lender has been deficient in its handling of a loan, the SBA office processing the purchase will attempt to reach an equitable resolution with the lender, which may involve the lender agreeing to a monetary adjustment in the amount of SBA's guaranty (referred to by SBA as a “repair”). However, SBA may consider a denial of its liability under its guaranty or litigation to recover funds SBA already paid under its guaranty to the lender (or secondary market holder) if the lender is not negotiating in good faith, the lender is unwilling to agree to a repair that reflects the harm caused to the SBA, or the lender's actions are sufficiently serious that a repair would be inappropriate.

SBA regulations at 13 CFR §120.524 describe when SBA will be released of liability on a loan guaranty. Lender also should consult the guaranty purchase procedures in SOP 50 50 4A, Chapters 9 and 10, and SOP 50 51 2A, Chapter 13.

Expiration of guaranty after maturity: If the lender fails to request purchase within 120 days after loan maturity, SBA is not legally obligated to purchase the guaranty. 13 C.F.R. § 120.524. Under certain circumstances, SBA may permit reinstatement of the guaranty and extension of the maturity (thereby extending the period during which the lender may request purchase). For example, reinstatement may be appropriate if the lender was actively servicing or liquidating the account with SBA knowledge or

concurrency, and inadvertently failed to timely request purchase or extend the loan maturity.