or nearly new.

(ii) Default or business failure that occurs more than 18 months after final disbursement

Under these circumstances, financial staff should consider a number of factors including length of time the borrower was in business; the relative size of the SBA loan compared to the business assets to be purchased; the type of assets purchased; normal depreciation or obsolescence of the assets; and whether there has been replacement of the assets with leased items, or by assets financed with purchase money security interest financing. Repair or full/partial denial may or may not be appropriate depending on the circumstances. An exercise of judgment is required.

23. Change of Ownership

In cases where whole businesses are purchased, asset values may not reflect fair market value and may bring little recovery at liquidation, even a short time after disbursement. Each case requires the exercise of judgment based on the condition of the assets when purchased and normal depreciation in the business operation prior to and subsequent to the change in ownership.

24. Borrower's Injection

Lenders are required to verify injections prior to disbursing loan proceeds and must maintain evidence of such verification in their loan files. Lenders are expected to use reasonable and prudent efforts to verify that equity is injected and used as intended, and failure to do so may warrant a repair or partial/full denial. Lenders must submit with each purchase request on a loan for which the loan authorization required an equity injection, documentation to show that they verified the equity injection. Generally, SBA staff will review this documentation only when the loan has experienced an early default or early loan problems, although SBA may review this documentation for other loans as well if circumstances warrant. SBA staff will consider the following in determining whether to seek a repair or recommend full/partial denial:

a. Cash Injection

Verifying a cash injection requires documentation such as a copy of a check along with evidence that the check was processed (e.g., at least one bank account statement dated before, but close to, disbursement showing that the funds were available and deposited into the borrower's account), or a copy of an escrow settlement accompanied by a bank account statement showing the injection into the business prior to disbursement. A promissory note, "gift letter" or financial statement alone is generally not sufficient evidence of cash injection.

For any cash injection that is greater than 1/3 of the loan amount or $200,000, whichever is less, the lender must also verify and document the source of the cash injection. If the cash injection is less than both of these amounts, the lender is required to verify and document only the existence of the cash injection, but not also its source.

If a shareholder loan is used as an equity injection, the lender must produce a full standby agreement, or evidence to show that loan payments were made by an entity other than the borrower. The lender must also present credible evidence to demonstrate that the borrower did not use 7(a) loan proceeds to fund the required injection, such as a bank statement showing that the money was available prior to the disbursement of the loan. The sufficiency of evidence from a lender to demonstrate verification of a cash injection depends upon the size of the injection and length of time that a borrower was in business, as discussed below.

b. Asset Injection

Asset injections may be more difficult to verify than cash injections. Evidence is often located in the lender's application for guaranty, in the borrower's financial statements, or in the SBA loan processor's write-up, as applicable. SOP 50 10 4 requires lenders to carefully determine the value of non-cash assets injected into the business. See Subpart A, Chapter 4, Paragraph 1(f)(4).

c. Length of Time in Business

If there is an early default or early loan problem and a significant cash injection (see discussion below in subparagraph (d)) is not properly documented, a direct link between business failure and the lack of injection should be assumed, and a full denial of liability may be appropriate. If the loan experienced early default or early loan problems, a lender's failure to verify a significant cash injection may be related to potential loss on the loan. If default occurs after 18 months from final disbursement, an exercise of judgment is required based upon an analysis of the cause of business failure and the length of time the business remained open. For example, if the business was in operation for several years after disbursement, the lender may be able to demonstrate that the lack of borrower's injection did not play a significant role in the failure. In this situation, a repair or partial denial in the amount of the unverified cash injection would generally not be appropriate.

d. Size of Injection

The amount of the required injection and the size of the loan should be compared. A relatively large injection is generally more instrumental to the business' success than a small injection. Lack of a small injection usually is not a significant factor in the failure of the business unless this failure is combined with a number of other lender deficiencies.

e. Partial Verification of Injection