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(1) Loan has a maturity of 15 years or more.

(2) Borrower makes a voluntary prepayment (or several prepayments in the aggregate) during any one of the first three successive 12 month periods following the first disbursement of the loan. Prepayment is defined as a payment of principal in excess of the amount due according to the amortization schedule.

(3) The prepayment (or several prepayments in the aggregate) is more than 25 percent of the highest outstanding principal balance of the loan in any one of the first three successive 12 month periods following the first disbursement.

(b) When all the conditions above exist, the following subsidy recoupment fees apply:

(1) If the prepayment is made during the first 12 month period after first disbursement, the charge is 5 percent of the total amount of all prepayments made during such period;

(2) If the prepayment is made during the second 12 month period after first disbursement, the charge is 3 percent of the total amount of all prepayments made during that period; and

(3) If the prepayment is made during the third 12 month period after first disbursement, the charge is 1 percent of the total amount of all prepayments made during that period.

[68 FR 51680, Aug. 28, 2003]

Subpart C—Special Purpose Loans

§ 120.300 Statutory authority.

Congress has authorized several special purpose programs in various subsections of section 7(a) of the Act. Generally, 7(a) loan policies, eligibility requirements and credit criteria enumerated in subpart B of this part apply to these programs. The sections of this subpart prescribe the special conditions applying to each special purpose program. As with other business loans, special purpose loans are available only to the extent funded by annual appropriations.

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DISABLED ASSISTANCE LOAN PROGRAM (DAL)

§ 120.310 What assistance is available for the disabled?

Section 7(a)(10) of the Act authorizes SBA to guarantee or make direct loans to the disabled. SBA distinguishes two kinds of assistance:

(a) *DAL-1*. DAL-1 Financial Assistance is available to non-profit public or private organizations for disabled individuals that employ such individuals; or

(b) *DAL-2*. DAL-2 Financial Assistance is available to:

(1) Small businesses wholly owned by disabled individuals; and

(2) Disabled individuals to establish, acquire, or operate a small business.

§ 120.311 Definitions.

(a) *Organization for the disabled* means one which:

(1) Is organized under federal or state law to operate in the interest of disabled individuals;

(2) Is non-profit;

(3) Employs disabled individuals for seventy-five percent of the time needed to produce commodities or services for sale; and

(4) Complies with occupational and safety standards prescribed by the Department of Labor.

(b) *Disabled individual* means a person who has a permanent physical, mental or emotional impairment, defect, ailment, disease or disability which limits the type of employment for which the person would otherwise be qualified.

§ 120.312 DAL-1 use of proceeds and other program conditions.

(a) DAL-1 applicants must submit appropriate documents to establish program eligibility.

(b) Generally, applicants may use loan proceeds for any 7(a) loan purposes. Loan proceeds may not be used:

(1) To purchase or construct facilities if construction grants and mortgage assistance are available from another Federal source; or

(2) For supportive services (expenses incurred by a DAL-1 organization to subsidize wages of low producers, health and rehabilitation services,

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management, training, education, and housing of disabled workers).

(c) SBA does not consider a DAL-1 organization to have a conflict of interest if one or more of its Associates is an Associate of the Lender.

§ 120.313 DAL-2 use of proceeds and other program conditions.

(a) The DAL-2 loan proceeds may be used for any 7(a) loan purposes.

(b) An applicant may use DAL-2 loan proceeds to acquire an eligible small business without complying with the change of ownership conditions in § 120.202.

(c) A DAL-2 applicant must submit evidence from a physician, psychiatrist, or other qualified professional as to the permanent nature of the disability and the limitation it places on the applicant.

§ 120.314 Resolving doubts about creditworthiness.

For the purpose of the DAL Program, SBA shall resolve doubts concerning the creditworthiness of an applicant in favor of the applicant. However, the applicant must present satisfactory evidence of repayment ability. Personal guarantees of Associates are not required for purposes of DAL-1 financial assistance.

§ 120.315 Interest rate and loan limit.

The interest rate on direct DAL loans is three percent. There is an administrative limit of \$150,000 on a direct DAL loan.

BUSINESSES OWNED BY LOW INCOME INDIVIDUALS

§ 120.320 Policy.

Section 7(a)(11) of the Act authorizes SBA to guarantee or make direct loans to establish, preserve or strengthen small business concerns:

(a) Located in an area having high unemployment according to the Department of Labor;

(b) Located in an area in which a high percentage of individuals have a low income inadequate to satisfy basic family needs; and

(c) More than 50 percent owned by low income individuals.

ENERGY CONSERVATION

§ 120.330 Who is eligible for an energy conservation loan?

SBA may make or guarantee loans to assist a small business to design, engineer, manufacture, distribute, market, install, or service energy devices or techniques designed to conserve the Nation's energy resources.

§ 120.331 What devices or techniques are eligible for a loan?

Eligible energy conservation devices or techniques include:

(a) Solar thermal equipment;

(b) Photovoltaic cells and related equipment;

(c) A product or service which increases the energy efficiency of existing equipment, methods of operation or systems which use fossil fuels, and which is on the Energy Conservation Measures list of the Secretary of Energy;

(d) Equipment producing energy from wood, biological waste, grain or other biomass energy sources;

(e) Equipment for cogeneration of energy, district heating or production of energy from industrial waste;

(f) Hydroelectric power equipment;

(g) Wind energy conversion equipment; and

(h) Engineering, architectural, consulting, or other professional services necessary or appropriate for any of the devices or techniques in paragraphs (a) through (g) of this section.

§ 120.332 What are the eligible uses of proceeds?

(a) *Acquire property.* The Borrower may use the loan proceeds to acquire land necessary for imminent plant construction, buildings, machinery, equipment, furniture, fixtures, facilities, supplies, and material needed to accomplish any of the eligible program purposes in § 120.330.

(b) *Research and development.* Up to 30% of loan proceeds may be used for research and development:

(1) Of an existing product or service; or

(2) A new product or service.

(c) *Working capital.* The Borrower may use proceeds for working capital

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for entering or expanding in the energy conservation market.

§ 120.333 Are there any special credit criteria?

In addition to regular credit evaluation criteria, SBA shall weigh the greater risk associated with energy projects. SBA shall consider such factors as quality of the product or service, technical qualifications of the applicant's management, sales projections, and financial status.

EXPORT WORKING CAPITAL PROGRAM (EWCP)

§ 120.340 What is the Export Working Capital Program?

Under the EWCP, SBA guarantees short-term working capital loans made by participating lenders to exporters (section 7(a)(14) of the Act). Loan maturities may be for up to three years with annual renewals. Proceeds can be used only to finance export transactions. Loans can be for single or multiple export transactions. An export transaction is the production and payment associated with a sale of goods or services to a foreign buyer.

§ 120.341 Who is eligible?

In addition to the eligibility criteria applicable to all 7(a) loans, an applicant must be in business for one full year at the time of application, but not necessarily in the exporting business. SBA may waive this requirement if the applicant has sufficient export trade experience or other managerial experience.

§ 120.342 What are eligible uses of proceeds?

Loan proceeds may be used:

- (a) To acquire inventory;
- (b) To pay the manufacturing costs of goods for export;
- (c) To purchase goods or services for export;
- (d) To support standby letters of credit;
- (e) For pre-shipment working capital; and
- (f) For post-shipment foreign accounts receivable financing.

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§ 120.343 Collateral.

A Borrower must give SBA a first security interest sufficient to cover 100 percent of the EWCP loan amount (such as insured accounts receivable or letters of credit). Collateral must be located in the United States, its territories or possessions.

§ 120.344 Unique requirements of the EWCP.

(a) An applicant must submit cash flow projections to support the need for the loan and the ability to repay. After the loan is made, the loan recipient must submit continual progress reports.

(b) SBA does not limit the amount of extraordinary servicing fees, as referenced in §120.221(b), under the EWCP.

(c) SBA does not prescribe the interest rates for the EWCP, but will monitor these rates for reasonableness.

INTERNATIONAL TRADE LOANS

§ 120.345 Policy.

Section 7(a)(16) of the Act authorizes SBA to guarantee loans to small businesses that are:

- (a) Engaged or preparing to engage in international trade; or
- (b) Adversely affected by import competition.

§ 120.346 Eligibility.

(a) An applicant must establish that:

- (1) The loan proceeds will significantly expand an existing export market or develop new export markets; or
 - (2) The applicant business is adversely affected by import competition; and
 - (3) Upgrading facilities or equipment will improve the applicant's competitive position.
- (b) The applicant must have a business plan reasonably supporting its projected export sales.

§ 120.347 Use of proceeds.

The Borrower may use loan proceeds to acquire, construct, renovate, modernize, improve, or expand facilities and equipment to be used in the United States to produce goods or services involved in international trade, and to develop and penetrate foreign markets.

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§ 120.348 Amount of guarantee.

SBA can guarantee up to \$1,250,000 for a combination of fixed-asset financing and working capital, supplies and EWCP assistance. The fixed-asset portion of the loan cannot exceed \$1,000,000 and the non-fixed-asset portion cannot exceed \$750,000.

QUALIFIED EMPLOYEE TRUSTS (ESOP)

§ 120.350 Policy.

Section 7(a)(15) of the Act authorizes SBA to guarantee a loan to a qualified employee trust ("ESOP") to:

- (a) Help finance the growth of its employer's small business; or
- (b) Purchase ownership or voting control of the employer.

§ 120.351 Definitions.

All terms specific to ESOPs have the same definition for purposes of this section as in the Internal Revenue Service (IRS) Code (title 26 of the United States Code) or regulations (26 CFR chapter I).

§ 120.352 Use of proceeds.

Loan proceeds may be used for two purposes.

(a) *Qualified employer securities.* A qualified employee trust may relend loan proceeds to the employer by purchasing qualified employer securities. The small business concern may use these funds for any general 7(a) purpose.

(b) *Control of employer.* A qualified employee trust may use loan proceeds to purchase a controlling interest (51 percent) in the employer. Ownership and control must vest in the trust by the time the loan is repaid.

§ 120.353 Eligibility.

SBA may assist a qualified employee trust (or equivalent trust) that meets the requirements and conditions for an ESOP prescribed in all applicable IRS, Treasury and Department of Labor (DOL) regulations. In addition, the following conditions apply:

- (a) The small business must provide the funds needed by the trust to repay the loan; and
- (b) The small business must provide adequate collateral.

§ 120.354 Creditworthiness.

In determining repayment ability, SBA shall not consider the personal assets of the employee-owners of the trust. SBA shall consider the earnings history and projected future earnings of the employer small business. SBA may consider the business and management experience of the employee-owners.

VETERANS LOAN PROGRAM

§ 120.360 Which veterans are eligible?

SBA may guarantee or make direct loans to a small business 51 percent owned by one or more of the following eligible veterans:

- (a) Vietnam-era veterans who served for a period of more than 180 days between August 5, 1964, and May 7, 1975, and were discharged other than dishonorably;
- (b) Disabled veterans of any era with a minimum compensable disability of 30 percent; or
- (c) A veteran of any era who was discharged for disability.

§ 120.361 Other conditions of eligibility.

(a) Management and daily operations of the business must be directed by one or more of the veteran owners whose veteran status was used to qualify for the loan.

(b) This direct loan program is available only if private sector financing and guaranteed loans are not available.

(c) A veteran may qualify only once for this program on a direct loan basis.

POLLUTION CONTROL PROGRAM

§ 120.370 Policy.

Section 7(a)(12) of the Act authorizes SBA to guarantee loans up to \$1,000,000 to an eligible small business to plan, design or install a pollution control facility. An applicant must meet the eligibility requirements for 7(a) loans.

LOANS TO PARTICIPANTS IN THE 8(A) PROGRAM

§ 120.375 Policy.

Section 7(a)(20) of the Act authorizes SBA to provide direct (unilaterally or together with Lenders) or guaranteed

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loans to firms participating in the 8(a) Program.

§ 120.376 Special requirements.

The following special conditions apply (otherwise, 7(a) loan eligibility criteria apply):

(a) The Director, Office of Business Development (“MED”) may waive the direct loan administrative ceiling of \$150,000, and raise it to \$750,000.

(b) The SBA portion of a guaranteed loan must not exceed \$750,000.

(c) The interest rate on a guaranteed loan shall be the same as on 7(a) guaranteed business loans. The interest rate on a direct loan shall be one percent less than on a regular direct loan.

(d) For a direct loan or SBA’s portion of an immediate participation loan, SBA shall subordinate its security interest on all collateral to other debt of the applicant.

§ 120.377 Use of proceeds.

The loan proceeds shall not be used for debt refinancing. Only a manufacturing concern may use loan proceeds for working capital.

DEFENSE ECONOMIC TRANSITION ASSISTANCE

§ 120.380 Program.

Section 7(a)(21) of the Act authorizes SBA to guarantee loans to help eligible small businesses transition from defense to civilian markets, or eligible individuals adversely impacted by base closures or defense cutbacks to acquire or open and operate a small business.

§ 120.381 Eligibility.

(a) *Eligible small businesses.* A small business is eligible if it has been detrimentally impacted by the closure (or substantial reduction) of a Department of Defense installation, or the termination (or substantial reduction) of a Department of Defense Program on which the small business was a prime contractor, subcontractor, or supplier at any tier.

(b) *Eligible individual.* An eligible individual, for purposes of this program, includes the following persons involuntarily separated from their position or voluntarily terminated under a pro-

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gram offering inducements to encourage early retirement:

(1) A member of the Armed Forces of the United States (honorably discharged);

(2) A civilian employee of the Department of Defense; or

(3) An employee of a prime contractor, sub-contractor, or supplier at any tier of a Department of Defense program.

(c) *Defense loan and technical assistance (DELTA).* The DELTA program provides financial and technical assistance to defense dependent small businesses which have been adversely affected by defense reductions. The goal of the program is to assist these businesses to diversify into the commercial market while remaining part of the defense industrial base. Complete information on eligibility and other rules is available from each SBA district office.

§ 120.382 Repayment ability.

SBA shall resolve reasonable doubts concerning the small business’ proposed business plan for transition to non-defense-related markets in favor of the loan applicant in determining the sound value of the proposed loan.

§ 120.383 Restrictions on loan processing.

Since greater risk may be associated with a loan to an applicant under this program, a Certified Lender or Preferred Lender shall not make a defense economic assistance loan under the PLP or CLP programs.

CAPLINES PROGRAM

§ 120.390 Revolving credit.

(a) CapLines finances eligible small businesses’ short-term, revolving and non-revolving working-capital needs. SBA regulations governing the 7(a) loan program govern business loans made under this program. Under CapLines, SBA generally can guarantee up to \$750,000.

(b) CapLines proceeds can be used to finance the cyclical, recurring, or other identifiable short-term operating capital needs of small businesses. Proceeds can be used to create current assets or used to provide financing against the current assets that already exist.

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BUILDERS LOAN PROGRAM

§ 120.391 What is the Builders Loan Program?

Under section 7(a)(9) of the Act, SBA may make or guarantee loans to finance small general contractors to construct or rehabilitate residential or commercial property for resale. This program provides an exception under specified conditions to the general rule against financing investment property. “Construct” and “rehabilitate” mean only work done on-site to the structure, utility connections and landscaping.

§ 120.392 Who may apply?

A construction contractor or home-builder with a past history of profitable construction or rehabilitation projects of comparable type and size may apply. An applicant may subcontract the work. Subcontracts in excess of \$25,000 may require 100 percent payment and performance bonds.

§ 120.393 Are there special application requirements?

(a) An applicant must submit documentation from:

(1) A mortgage lender indicating that permanent mortgage money is available to qualified purchasers to buy such properties;

(2) A real estate broker indicating that a market exists for the proposed building and that it will be compatible with its neighborhood; and

(3) An architect, appraiser or engineer agreeing to make inspections and certifications to support interim disbursements.

(b) The Borrower may substitute a letter from a qualified Lender for one or more of the letters.

§ 120.394 What are the eligible uses of proceeds?

A Borrower must use the loan proceeds solely to acquire, construct or substantially rehabilitate an individual residential or commercial building for sale. “Substantial” means rehabilitation expenses of more than one-third of the purchase price or fair market value at the time of the application. A Borrower may use up to 20 percent of the proceeds to acquire land,

and up to 5 percent for community improvements such as curbs and sidewalks.

§ 120.395 What is SBA’s collateral position?

SBA will require a lien on the building which must be in no less than a second position.

§ 120.396 What is the term of the loan?

The loan must not exceed sixty (60) months plus the estimated time to complete construction or rehabilitation.

§ 120.397 Are there any special restrictions?

The borrower must not use loan proceeds to purchase vacant land for possible future construction or to operate or hold rental property for future rehabilitation. SBA may allow rental of the property only if the rental will improve the ability to sell the property. The sale must be a legitimate change of ownership.

Subpart D—Lenders

§ 120.400 Loan Guarantee Agreements.

SBA may enter into a Loan Guarantee Agreement with a Lender to make deferred participation (guaranteed) loans. Such an agreement does not obligate SBA to participate in any specific proposed loan that a Lender may submit. The existence of a Loan Guarantee Agreement does not limit SBA’s rights to deny a specific loan or establish general policies. *See also* §§ 120.441(b) and 120.451(d) concerning Supplemental Guarantee Agreements.

PARTICIPATION CRITERIA

§ 120.410 Requirements for all participating Lenders.

A Lender must:

(a) Have a continuing ability to evaluate, process, close, disburse, service and liquidate small business loans;

(b) Be open to the public for the making of such loans (not be a financing subsidiary, engaged primarily in financing the operations of an affiliate);

(c) Have continuing good character and reputation, and otherwise meet