

## **OVERVIEW OF 1998 CHANGES TO SBA 7(a) NOTE, 504 NOTE, AND GUARANTEES**

SBA is issuing updated versions of its 7(a) Note, 504 Note, and Unconditional Guarantee, and is introducing a new form, the Unconditional Limited Guarantee (the "Notes" and "Guarantees"). They can be used beginning October 15, 1998 and will be mandatory on November 15, 1998.

For specific instructions and policy guidance for using the documents, refer to the *SBA Inst 147 (9/98)*, *SBA Inst 1505 (9/98)*, and *SBA Inst 148/148L (9/98)*.

### **CHANGES APPLICABLE TO ALL DOCUMENTS**

- A. Language and Format. The documents were rewritten in plain language, with updated appearance and style. They use short sentences, short paragraphs, vertical lists, and numbers for individual elements.
- B. Information Grid. This grid is located at the top of the documents. The completed grid will be an easy reference point for important information about the loan, such as the loan number, loan amount and the borrower's name. Lenders must carefully complete the grid. The grid is more than just information; the items in the grid constitute the definitions of Borrower, Guarantor, Operating Company, Lender, and CDC.
- C. Federal Law. The Note and Guarantees state that federal law will apply when SBA holds the documents. The provision also advises signers that they may not assert state or local law to deny any obligation, defeat SBA's claims, or preempt federal law.
- D. Successors and Assigns. Borrower and Guarantor include successors; Lender and CDC include successors and assigns. SBA will have the rights of the Lender or CDC when the Note is assigned to SBA.
- E. Oral Statements Not Binding. This paragraph limits claims based on oral representations, such as equitable estoppel. It also notifies the borrower or guarantor of the parole evidence rule, which bars introduction of evidence of prior negotiations to vary the terms of a written contract.
- F. Waivers. The documents include specific waivers of suretyship defenses.
- G. Requirement to Sign Documents. Borrowers and Guarantors are required to sign any additional documents needed to allow the Lender or CDC to acquire, perfect, or maintain its liens on collateral.
- H. State Specific Provisions. The documents have a space to insert the state-specific provisions required by SBA's 7(a) National Authorization and 504 National Authorization.
- I. Signatures. The documents no longer contain lines for signatures. Lenders must complete the signature blocks.

## **CHANGES TO BOTH NOTES**

- A. **Borrower.** “Borrower” replaces the term “Undersigned” used in the previous SBA Notes.
- B. **Definitions.** The definition and references to “Indebtedness” in the previous SBA Notes are eliminated. A definition of “Guarantor” is added and the definition of “Collateral” no longer includes guarantees. There is a new defined term, “Loan Documents.”
- C. **New or Changed Events of Default.** Default provisions are found in Paragraph 5 in the 7(a) Note, and in Paragraph 7 in the 504 Note. Several provisions have changed:
1. Non-payment events of default in this section also apply to the Operating Company. (See the introductory paragraph.)
  2. The Notes include a cross-default provision. Default by the Borrower on any other loan held by the Lender is a default under the 7(a) Note. In the 504 Note, a default on any other SBA loan is default under the 504 Note. (See Subparagraph B.)
  3. A breach of any agreement with any other creditor or a failure to pay any taxes when due will be a default under the Note if the Lender determines that the incident may materially affect the Borrower’s ability to perform the Note’s obligations. (See Subparagraphs F and G.)
  4. An adverse change in the Borrower’s financial condition or business operation will be a default under the Note if the Lender determines that the incident may materially affect the Borrower’s ability to pay the Note. (See Subparagraph K.)
  5. Bankruptcy or other formal insolvency proceedings are events of default, but they will not automatically accelerate the indebtedness. (See Subparagraphs H, I, and J.)
  6. The Borrower is in default if there is a civil or criminal action that the Lender believes may materially affect the Borrower’s ability to pay the Note. (See Subparagraph M.)
- D. **Lender’s Rights Upon Default.** The Lender may accelerate the Note and require the entire loan to be repaid immediately if there is a default. (Paragraph 6 in the 7(a) Note, and 8 in the 504 Note.) The Lender may liquidate any collateral, and collect the debt from anyone obligated to repay the loan. Although this paragraph gives the Lender broad powers to collect on the loan and dispose of the collateral, any action taken must be consistent with state law. This may require that notice be given or consent obtained. The Lender is not obligated to exercise any remedy upon default and may delay foreclosure without forfeiting that remedy. (Paragraph 10 D in the 7(a) Note, and 12 D in the 504 Note.)
- E. **Lender’s General Powers.** Paragraph 7 in the 7(a) Note and Paragraph 9 of the 504 Note describe Lender’s general powers. The Lender may exercise these powers at any time during the term of the loan, even if the Borrower is not in default. Subsection B allows the Lender to incur expenses to protect the collateral and enforce the Note. These expenses include payment of delinquent taxes, reasonable attorney’s fees, environmental remediation costs, and other items. The Lender may add such expenses to the Note balance or may require immediate payment from the borrower.

## **CHANGES SPECIFIC TO THE 504 NOTE**

- A. Items that are blank at signing. The 504 Note states that the interest rate, the P & I Amount, and the Monthly Payment are blank when the Note is signed. The Borrower gives the CDC, the Servicing Agent, and SBA the right to complete the terms. (See the asterisked items under the information grid, and paragraph 12 B.)
- B. Funding Date. The term “Funding Date” replaces “date of Debenture” in the 504 Note as a more logical term to explain when the Note is funded and interest begins to accrue.
- C. Payment Amounts. The terms P & I amount (principal and interest amount) and Monthly Payment are new or revised. The P & I amount is the amount needed to amortize the Note. The Monthly Payment is the P & I amount plus the monthly fees. (See the items under the Information Grid and Paragraph 3.)
- D. Definitions. The 504 Note has new definitions for “Debenture,” “Servicing Agent Agreement,” and “Servicing Agent.” (See Paragraph 2.)
- E. Right to Prepay and Prepayment Premium. The pre-payment provisions give the borrower additional information about the right to prepay, amount needed to prepay, and the prepayment premium.

## **CHANGES TO THE UNCONDITIONAL GUARANTEE**

- A. The spelling of the word “Guaranty” is replaced with “Guarantee,” consistent with SBA’s regulations.
- B. New Name. The “U.S. Small Business Administration (SBA) Guaranty,” is now the “Unconditional Guarantee.” The SBA Form number remains the same, Form 148.
- C. Terms Grouped. The Guarantee is organized by logical subject areas.
- D. Waivers. There are expanded waiver provisions.
- E. Federal Law. This section replaces the reference in the old Guaranty to SBA’s regulations at Part 101.
- F. Modification of Note. The Guarantees provide that Lenders may modify the Note and other Loan Documents without a Guarantor’s consent, except to increase the amounts due under the Note. (Paragraph 4.A. in the Unconditional Guarantee, and 5.A. in the Unconditional Limited Guarantee.) If a Lender modifies the Note amount to increase it without the Guarantor’s consent, then the Guarantor will not be liable for the increased amounts and related interest and expenses, but will remain liable for the amounts due under the terms of the original Note. (Paragraph 6. C.14. in the Unconditional Guarantee, and 7.C.14. in the Unconditional Limited Guarantee.) Consent of the Guarantor is not needed for interest and items such as collection expenses, attorney’s fees, and payment of property taxes, to be added to the Note balance. The terms of the Note allow such items to be added.

- G. Collateral. The portion of the old Guaranty that required Lenders to list the collateral securing the Guaranty has been eliminated. There is a new section requiring the Guarantor to preserve the collateral securing the Guarantee. (Paragraph 7 in the Unconditional Guarantee, and 8 in the Unconditional Limited Guarantee.)
- H. General Provisions. There are several new terms in “General Provisions.” (Paragraph 9 in the Unconditional Guarantee, and 10 in the Unconditional Limited Guarantee.)
1. The Guarantor agrees to pay all expenses incurred to enforce the Guarantee, including attorney’s fees. (Paragraph 9.A. in the Unconditional Guarantee, and 10.A. in the Unconditional Limited Guarantee.)
  2. There is a severability clause to ensure that the remainder of the Guarantee is enforceable even if one provision is deemed unenforceable. (Paragraph 9.I. in the Unconditional Guarantee, and 10.I. in the Unconditional Limited Guarantee.)
  3. There is also a statement of consideration. (Paragraph 9.J. in the Unconditional Guarantee, and 10.J. in the Unconditional Limited Guarantee.)
- I. The Guarantor acknowledges all terms of the Note and the Guarantee by signing. (Paragraph 11 in the Unconditional Guarantee, and 12 in the Unconditional Limited Guarantee.)

### **THE NEW UNCONDITIONAL LIMITED GUARANTEE**

This is a new document, SBA Form 148L, but other than the addition of Paragraph 4, “Guarantee Limitation,” the text in this document is almost identical to the text in the Unconditional Guarantee. The new sub-paragraphs in Paragraph 4 contain several options for guarantee limitations. Use the Unconditional Limited Guarantee only when needed (see *SBA Inst 148/148L*). Absent a need for a limited guarantee, use the full guarantee (Unconditional Guarantee, Form 148).

Select only one limitation option for any one Guarantor. The options include limitations based on loan-balance reduction, principal reduction, amount paid by the Guarantor, percentage of loan, time, collateral, and community property or spousal interest.