



State of Washington

**DEPARTMENT OF FINANCIAL INSTITUTIONS
DIVISION OF CREDIT UNIONS**

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October 30, 2017

DCU Interpretive Letter I-17-03 (replaces I-14-01)

To: All Washington State Chartered Credit Unions

From: Linda Jekel, Director of Credit Unions

Subject: #1 Whether an SBA advance loan commitment (specifically on a SBA 504 program loan) is exempt from being considered a member business loan (MBL) under WAC 208-460-010; and

#2 If this loan is not exempt from being considered an MBL, is a SBA 504 program loan exempt from the MBL collateral and security requirements under WAC 208460-060.

Questions

Question #1: The Division of Credit Unions was asked whether a credit union loan made based on receipt of a Small Business Administration (SBA) 504 advance loan program commitment would be exempt from being considered a member business loan (MBL). Specifically, we were asked for a clarification on the interpretation of WAC 208-460-010(2)(d), which reads, “(2) Exemptions. The following are not member business loans... (d) A business purpose loan where a federal or state agency (or any political subdivision of a state) fully insures repayment or fully guarantees repayment, or provides and advance commitment to purchase in full.”

Question #2: If this loan is not considered exempt from being counted an MBL, is the loan exempt from the MBL collateral and security requirements under WAC 208-460-060, if the credit union is in receipt of a SBA 504 advance loan program commitment and requires the borrower to pay down the credit union’s loan from the proceeds of the second mortgage loan that has the SBA 504 program guarantee debenture.

Analysis

#1 Is the Credit Union's SBA 504 Program Loan Considered Exempt from Being an MBL?

Typically, a SBA 504 program loan has the following three elements:

1. A senior lien from a private sector lender covering up to 50% of the project cost;
2. A second mortgage secured with a junior lien from a second mortgage lien from a SBA certified development company (backed by a 100% SBA guaranteed debenture); and
3. A contribution of at least 10% equity from the borrower.¹

A SBA 504 advance loan commitment is a commitment from a certified development company (CDC) to fund a SBA guaranteed subordinate debenture (similar to a second mortgage) up to 40% of the SBA 504 program project costs. Because the credit union's first mortgage loan is not backed by a SBA guarantee, it is not exempt under WAC 208-460-010(2) (d). Note: Only the second mortgage loan issued by a certified development company is backed by a SBA guaranteed debenture.

#2 Is the Credit Union's SBA 504 Program Loan Exempt from the WAC 208-460-060 Collateral and Security Requirements?

The SBA 504 program loan may be considered exempt from the MBL collateral and security requirements of WAC 208-460-060, under certain conditions. WAC 208-460-060(2) (b) reads, "In the case of a member business loan secured by collateral on which the credit union will have a first lien, you may grant the loan with a LTV ratio in excess of eighty percent only when the value in excess of eighty percent is: (b) Insured or guaranteed, or subject to an advance commitment to purchase, by any federal or state agency (or a political subdivision of a state)." Note: The SBA advance commitment for a 100% SBA guaranteed debenture for a CDC issued second mortgage loan must be in place prior to the loan origination for the credit union to be exempt from the collateral and security requirements under WAC 208-460-060. It is our understanding that an SBA advanced commitment letter is usually issued prior to the first mortgage loan origination.

¹ SBA document titled "504 Loan Refinancing Program" that is available at <http://www.sba.gov/content/504-loanrefinancing-program-0>.

The analysis in the previous paragraphs is consistent with an NCUA legal opinion letter dated August 24, 2009.² This legal opinion letter reads, “You have asked if the exemption from the collateral and security requirements in NCUA’s member business loan (MBL) rule for loans as part of an SBA guaranteed loan program includes loans made under SBA’s 504 loan program. Yes, the exemption applies to SBA 504 loans.”

Once the CDC issued second mortgage loan is funded and the funds are used to reduce the first lien loan held by the credit union, the loan-to-value ratio for the credit union originated loan under the SBA 504 program would drop to 50% or less. However, the credit union’s first mortgage loan is not guaranteed for repayment by the SBA.

What about other SBA guaranteed loan programs, such as the SBA 7(a) program?

The SBA 7(a) loan program is a direct guarantee program, whereby the SBA guarantees a percentage of the loan, if the SBA requirements are met.

Additionally, staying consistent with the interpretation provided earlier in this letter regarding SBA 504 program loans, a credit union’s SBA 7(a) guaranteed loan with a guarantee already in effect or an advanced commitment to guarantee in place is exempt from the collateral and security requirements under WAC 208-460-060.

Conclusions

1. An SBA 504 program loan originated by a Washington state chartered credit unions is not exempt from being considered an MBL under WAC 208-460-010(2)(d).
2. An SBA 504 program loan originated by a Washington state chartered credit union will be exempt from the collateral and security requirements under WAC 208-460-060, if an SBA advance commitment for the second mortgage loan debenture guarantee on a CDC issued loan is in place prior to loan origination.
3. A SBA 7(a) guaranteed loan is exempt from the collateral and security requirements under WAC 208-460-060, if the guarantee is already in effect or an advanced commitment to guarantee is in place.

It is important that credit unions administer their SBA loan programs in a safe and sound manner, and not rely heavily on the SBA program guarantee or debenture. SBA guarantees can be lost or reduced due, if the SBA lending and authorization requirements are not met. Prudent management and control over an SBA lending program is fundamental to its success.

² NCUA legal opinion issued by Sheila A. Albin, Associate General Counsel titled “Collateral and Security Requirements for Small Business Administration (SBA) 504 Program Loans. This document is available at <http://www.ncua.gov/Legal/Pages/OL2009-0661.aspx>.

Credit union originated loans under the SBA 504 program are still subject to the MBL loans-to-one borrower limitation, the construction and develop (C&D) aggregate loan limitation, and the MBL aggregate limitation.

For any questions concerning this Interpretive Letter, contact Doug Lacy-Roberts, Program Manager, at Doug.Lacy-Roberts@dfi.wa.gov or (360) 902-8753.

The Division of Credit Unions does not provide legal advice. This interpretation is based on the facts as presented to the Division of Credit Unions and is provided as general guidance only, and is not a substitute for legal advice given to a credit union.