



## SBA's REMODELED EPC/OC RULE: A GOOD THING FOR BORROWERS ... WHAT YOU NEED TO KNOW

EPC/OC a fixer upper? Not at all. The structure is sound. But SBA's latest fixes to the Eligible Passive Rule (EPC/OC Rule) are more than paint and paper. Regulatory changes that became effective in late September loosen the ties affecting 7(a), 504, and all SBA business loan programs in three significant ways: 1) use of proceeds; 2) terms of the EPC/OC lease; and; 3) identification of guarantors, all resulting in improved credit quality for lenders.

Let's take a look at the two key fixes: the expanded use of loan proceeds in changes of ownership, and ways Eligible Passive Companies (EPCs) and Operating Companies (OCs) can increase their pool of guarantors.

**Expanded use of loan proceeds: How it Was.** SBA's hard-and-fast rule restricted an EPC's use of loan proceeds to acquiring or leasing, improving or renovating real or personal property they then leased to one or more Operating Companies. Under the rule, EPCs/OCs weren't eligible to apply for SBA loans for other purposes. In fact, financing change of ownership within an EPC was strictly prohibited. This posed a hardship, making it difficult to grow a business.

**What's New.** The amendment provides financing that wasn't available. The best example may be how the changes can assist a family business to transition ownership to the next generation. Take the case of a family business where the parents own 50 percent of the EPC/OC and their children own the other 50 percent. Now, the parents want to pass their share of both entities to the kids. This change allows the children to apply for an SBA loan to finance the buy-out of the EPC. *Let's make it clear: eligibility for SBA financing is internal, available only to existing owners of the EPC/OC.*

**Guarantors: How it Was.** Under the old SBA regulation, each required guarantor of a loan had to own at least 20 percent of the EPC *and* the OC.

**What's New.** Now, each guarantor need only own at least 20 percent of the EPC *or* the OC to guarantee the loan. And importantly, the new rule expands the pool of guarantors, allowing other individuals or entities to be full or limited guarantors regardless of their percentage of ownership. Taking on minority guarantors bolsters the credit quality of a loan.

Watch for more details on the revised regulation in the upcoming SOP 50 10 J due out soon. So stay tuned. And for all things SBA: [Contact JRB.](#)

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