

## § 120.120

the loan (the trustee shall execute the guarantee on behalf of any trust).

(b) *Additional conditions that apply to trusts.* The eligibility status of the trustor will determine trust eligibility. All donors to the trust will be deemed to have trustor status for eligibility purposes. A trust qualifying as an Eligible Passive Company may engage in other activities as authorized by its trust agreement. The trustee must warrant and certify that the trust will not be revoked or substantially amended for the term of the loan without the consent of SBA. The trustor must guarantee the loan. For purposes of this section, the trustee shall certify to SBA that:

- (1) The trustee has authority to act;
- (2) The trust has the authority to borrow funds, pledge trust assets, and lease the property to the Operating Company;
- (3) The trustee has provided accurate, pertinent language from the trust agreement confirming the above; and
- (4) The trustee has provided and will continue to provide SBA with a true and complete list of all trustors and donors.

[61 FR 3235, Jan. 31, 1996; 61 FR 7986, Mar. 1, 1996, as amended at 64 FR 2117, Jan. 13, 1999]

### USES OF PROCEEDS

#### § 120.120 What are eligible uses of proceeds?

A small business must use an SBA business loan for sound business purposes. The uses of proceeds are prescribed in each loan's Authorization.

(a) A Borrower may use loan proceeds from any SBA loan to:

- (1) Acquire land (by purchase or lease);
- (2) Improve a site (e.g., grading, streets, parking lots, landscaping), including up to 5 percent for community improvements such as curbs and sidewalks;
- (3) Purchase one or more existing buildings;
- (4) Convert, expand or renovate one or more existing buildings;
- (5) Construct one or more new buildings; and/or
- (6) Acquire (by purchase or lease) and install fixed assets (for a 504 loan, these assets must have a useful life of at

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least 10 years and be at a fixed location, although short-term financing for equipment, furniture, and furnishings may be permitted where essential to and a minor portion of the 504 Project).

(b) A Borrower may also use 7(a) and microloan proceeds for:

- (1) Inventory;
- (2) Supplies;
- (3) Raw materials; and
- (4) Working capital (if the Operating Company is a co-Borrower with an Eligible Passive Company, part of the loan proceeds may be applied for working capital if used for that purpose only by the Operating Company).

(c) A Borrower may use 7(a) loan proceeds for refinancing certain outstanding debts.

#### § 120.130 Restrictions on uses of proceeds.

SBA will not authorize nor may a Borrower use loan proceeds for the following purposes (including the replacement of funds used for any such purpose):

- (a) Payments, distributions or loans to Associates of the applicant (except for ordinary compensation for services rendered);
- (b) Refinancing a debt owed to a Small Business Investment Company ("SBIC");
- (c) Floor plan financing or other revolving line credit, except under § 120.390;
- (d) Investments in real or personal property acquired and held primarily for sale, lease, or investment (except for a loan to an Eligible Passive Company or to a small contractor under § 120.310);
- (e) A purpose which does not benefit the small business; or
- (f) Any use restricted by §§ 120.201 through 120.203 and 120.884 (specific to 7(a) loans and 504 loans respectively).

#### § 120.131 Leasing part of new construction or existing building to another business.

(a) If the SBA business loan involves the construction of a new building, a Borrower may lease up to 33 percent of the Rentable Property for a short term to any third party if reasonable growth projections show that the Borrower will need additional space within three

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years and will use all of the additional space within ten years. If the Borrower is an Eligible Passive Company leasing 100 percent of the Project space to one or more Operating Company, the Operating Company, or Operating Companies together, may sublease up to 33 percent of the Rentable Property to a third party under the same conditions. (See §120.870(c) for an exception with respect to 504 Projects.)

(b) If the SBA business loan involves the acquisition, renovation, or reconstruction of an existing building, the Borrower may lease up to 49 percent of the Rentable Property long term. If the Borrower is an Eligible Passive Company leasing 100 percent of the Project space to one or more Operating Companies, the Operating Company, or Operating Companies together may sublease up to 49 percent of its Rentable Property to a third party under the same conditions. (For 504 loans, see §120.871).

[64 FR 2117, Jan. 13, 1999; 64 FR 27445, May 20, 1999]

### ETHICAL REQUIREMENTS

#### § 120.140 What ethical requirements apply to participants?

Lenders, Intermediaries, CDCs, and Associate Development Companies (“ADCs”) (in this section, collectively referred to as “Participants”), must act ethically and exhibit good character. Ethical indiscretion of an Associate of a Participant or a member of a CDC will be attributed to the Participant. A Participant must promptly notify SBA if it obtains information concerning the unethical behavior of an Associate. The following are examples of such unethical behavior. A Participant may not:

- (a) Self-deal;
- (b) Have a real or apparent conflict of interest with a small business with which it is dealing (including any of its Associates or an Associate’s Close Relatives) or SBA;
- (c) Own an equity interest in a business that has received or is applying to receive SBA financing (during the term of the loan or within 6 months prior to the loan application);

(d) Be incarcerated, on parole, or on probation;

(e) Knowingly misrepresent or make a false statement to SBA;

(f) Engage in conduct reflecting a lack of business integrity or honesty;

(g) Be a convicted felon, or have an adverse final civil judgment (in a case involving fraud, breach of trust, or other conduct) that would cause the public to question the Participant’s business integrity, taking into consideration such factors as the magnitude, repetition, harm caused, and remoteness in time of the activity or activities in question;

(h) Accept funding from any source that restricts, prioritizes, or conditions the types of small businesses that the Participant may assist under an SBA program or that imposes any conditions or requirements upon recipients of SBA assistance inconsistent with SBA’s loan programs or regulations;

(i) Fail to disclose to SBA all relationships between the small business and its Associates (including Close Relatives of Associates), the Participant, and/or the lenders financing the Project of which it is aware or should be aware;

(j) Fail to disclose to SBA whether the loan will:

(1) Reduce the exposure of a Participant or an Associate of a Participant in a position to sustain a loss;

(2) Directly or indirectly finance the purchase of real estate, personal property or services (including insurance) from the Participant or an Associate of the Participant;

(3) Repay or refinance a debt due a Participant or an Associate of a Participant; or

(4) Require the small business, or an Associate (including Close Relatives of Associates), to invest in the Participant (except for institutions which require an investment from all members as a condition of membership, such as a Production Credit Association);

(k) Issue a real estate forward commitment to a builder or developer; or

(l) Engage in any activity which taints its objective judgment in evaluating the loan.