



**MANAGEMENT COMMITTEE**

**PRESIDENT**  
JEFFREY GOLDRICH  
SLR BUSINESS CREDIT

**FIRST VICE PRESIDENT**  
PETER YORK  
J.P. MORGAN SECURITIES LLC

**VICE PRESIDENT - FINANCE**  
JENNIFER PALMER  
GERBER FINANCE, INC.

**CO-GENERAL COUNSEL**  
JONATHAN HELFAT  
OTTERBOURG P.C.

**CO-GENERAL COUNSEL**  
BOBBI ACORD NOLAND  
PARKER, HUDSON, RAINER &  
DOBBS LLP

**CEO & SECRETARY**  
RICHARD GUMBRECHT,  
SECURED FINANCE NETWORK

July 28, 2021

Mr. Daniel Krupnick  
United States Small Business Administration  
Washington, D.C.

Re: Covid-19 Economic Injury Disaster Loan Program

Dear Mr. Krupnick:

Thank you for meeting with us and discussing the concerns of our members relating to the SBA's COVID-19 Economic Injury Disaster Loan ("EIDL") program.

As we advised the SBA in our prior correspondence, the Secured Finance Network ([www.sfnet.com](http://www.sfnet.com)) is the international trade organization of the asset-based lending industry, founded in 1944, representing the asset-based lending, factoring, trade and supply chain finance industries, with over 260 member organizations throughout the United States, Canada and around the world. Our members include regulated money center banks, independent finance companies, community banks, factors and leasing companies which provide hundreds of billions of dollars annually in working capital to thousands of small businesses throughout the United States.

SFNet supports the overarching goal of the SBA's COVID-19 EIDL program of providing as much working capital as possible to the small business borrower adversely affected by COVID-19. While it is a common misconception, the SBA's COVID-19 EIDL program does not make loans exclusively to small businesses that cannot secure working capital elsewhere. Many of our members offer loans and advances to these very same businesses and in amounts that are far in excess of the EIDL facility, which in and of itself would be insufficient as a standalone facility to provide these borrowers with the necessary capital required to sustain their businesses. Therefore, it is our assumption that the SBA envisioned that the COVID-19 EIDL facility and the private lending facility would work "hand in hand" in order to provide the small business owner who is eligible for a COVID-19 EIDL with the maximum amount of working capital possible.

Unfortunately, certain basic terms, as contained in most private credit agreements are in direct conflict with certain basic terms of the EIDL.

By way of example:

- a. As the EIDL is, by its terms, a collateralized facility; in almost all instances it conflicts with the terms of the private lender's credit agreement, which is also a collateralized facility, and which provides that the borrower will not permit any other liens on the borrower's assets whether senior, junior or *pari passu* without the private lender's consent. As a result, the EIDL would cause an immediate default under the lender's credit agreement preventing any further lending by the private lender without the borrower first obtaining the SBA's consent. To waive this default, the SBA would have to be willing to subordinate its liens and claims to those of the private lender. As things stand today, this is a very difficult and time-consuming process, if granted at all.
- b. The EIDL requires that its borrower not sell or transfer any collateral (except inventory in the ordinary course of business) without the prior written consent of the SBA. As most private lenders, pursuant to the term of their respective credit agreements, take an assignment of their borrower's accounts receivable; this would be yet another default under the private lender's credit agreement which would, again, prevent further lending by the private lender unless the SBA were willing to subordinate its liens and claims.
- c. A final example is the requirement under the terms of the EIDL the borrower will neither seek nor accept future advances under any superior liens on the collateral securing the EIDL without the prior written consent of the SBA. This prohibition would, again, cause an immediate default under the private lender's credit agreement which, absent the SBA agreeing to subordinate, would prevent further lending by the private lender. This requirement would also prevent a "new" lender from making loans to a borrower with an existing EIDL.

To solve these issues in favor of greater funds being made available to the EIDL borrower, the SBA has been willing in principle to subordinate its EIDL facility in favor of the borrower's private lender. However, in practice, this is not occurring except in limited circumstances.

Due the disparate administration of the EIDL program by the various SBA regional administrators, the requested subordination agreements have ranged from acceptable to totally unacceptable.

A few examples may help illustrate the point.

It appears that the Texas regional offices of the SBA are willing to agree to subordination language that is substantially similar to the terms requested by the private lender while the Birmingham, Alabama office is not and has its own form of subordination, which is narrow in scope and unacceptable to most lenders as this regional office will only subordinate the EIDL facility to the private lender's liens on "accounts" and "inventory," but not "proceeds," which not only is contrary to the provisions of the UCC, but provides little, if any, protection for the private lender. However, these terms are "non-negotiable" according to the Birmingham regional administrator.

Other regional offices of the SBA require a partial pay down of the EIDL before agreeing to consider the requested subordination.

If this were not enough, other regional offices provide that the form of subordination must provide that the subordination is void if the SBA is not given 30 days written notice upon an event of default occurring under the terms of the private credit agreement before the lender can take any enforcement actions as provided for in its credit agreement. Waiting the thirty days works against the SBA's best interests and the private lender's best interest as it allows, for example, a borrower with fraudulent

intent to circumvent the previously agreed upon collection procedures to its own uses with the private lender and the SBA being unable to stop the dissipation of the collateral for 30 days.

As a result of this varied treatment of subordination requests, the EIDL borrower is being denied access to the much-needed funds, which otherwise would be available from its private lender. And this is not the only impediment to the requested subordination language. The regional offices uniformly take weeks and sometimes months to consider granting the requested subordination. Therefore, even if the requested subordination agreement is eventually forthcoming in a form acceptable to the private lender, it may come too late to be of maximum value as few borrowers have the ability to wait until the SBA has finished its process.

We would therefore suggest that the SBA consider adopting a uniform subordination agreement to be used nationwide. To adopt such a form would not require any statutory or regulatory changes. We enclose such a form (attached and below), which **has been previously approved by the SBA** in at least one of its regional offices and is also acceptable to our members. We look forward to discussing adopting such a form at your earliest convenience.

Finally, we would further ask the SBA to consider taking action relative to the unintended consequences of not monitoring whether the EIDL is being granted and used for its intended purpose. As the SBA has purposely made obtaining an EIDL relatively simple and provided repayment terms that are extraordinarily liberal (30 years) the cost of carrying the EIDL on the borrower's books given the 3.75% interest carry is minimal. As we discussed, certain borrowers are taking advantage of the program not for its intended purpose but as a reserve (call it a "rainy day fund") to be used sometime in the future for non-COVID-19 related capital needs.

This ability to keep these funds "on the sidelines" for a future non COVID-19 use is depriving the private sector of providing working capital to its borrowers at a market rate of interest on market terms in favor of an unintended government subsidy that bears significant repayment risk to taxpayers. We hope that future allocations under the program, particularly as the SBA considers increasing its loan thresholds, take this into consideration in favor of existing capital sources.

Thank you for the opportunity of allowing SFNet to set forth its observations and proposal for a uniform nationwide subordination agreement which, in our opinion, would provide the COVID-19 EIDL borrower with the greatest amount of working capital.

Sincerely,

A handwritten signature in black ink, appearing to read "R. Gumbrecht", with a long horizontal line extending to the right.

Richard Gumbrecht  
Chief Executive Officer  
Secured Finance Network

## **SUBORDINATION AGREEMENT**

THIS SUBORDINATION AGREEMENT, dated as of \_\_\_\_\_, 2021 (this "Agreement") is by and between U.S. SMALL BUSINESS ADMINISTRATION (hereinafter referred to as the "SBA") and \_\_\_\_\_ (hereinafter referred to as the "Bank").

\_\_\_\_\_, (the "Debtor") is indebted to the SBA pursuant to extensions of credit. In order to secure the full repayment of all sums due in connection with such extensions of credit, the SBA has perfected a security interest in the Collateral (as defined below) under the Uniform Commercial Code as in effect in the State of \_\_\_\_\_ from time to time (the "Uniform Commercial Code").

The Bank has granted to the Debtor a term loan/line of credit in the initial principal amount of \_\_\_\_\_ 00/100 Dollars (\$\_\_\_\_\_) (hereinafter the "Bank Credit Facility"). The Bank, in connection with such credit facilities and other extensions of credit, has perfected, or will perfect, its security interest under the Uniform Commercial Code in all assets and personal property of the Debtor which shall include, but not necessarily be limited to, the Collateral.

The Bank and the SBA desire to establish the priorities of their respective security interests in the Collateral pursuant to the terms and provisions of this Agreement.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, the parties hereto agree as follows:

Incorporation of Recitals. Recitals. A through C, above, are incorporated herein by this reference, and the parties acknowledge and agree that the information recited above is true and correct.

Definition of Collateral. "Collateral" means all of the following described personal property of the Debtor, whether now or hereafter existing or now owned or hereafter acquired and wherever located, of every kind and description, including all accounts receivable, inventory, furniture, fixtures, and machinery & equipment, excluding automotive, together with all substitutions, accessions, additions, and the proceeds and products thereof.

Lien Subordination. Notwithstanding anything to the contrary, the SBA hereby acknowledges and agrees that the security interest and lien of the Bank in the Collateral is senior to and has priority over the security interest and lien of the SBA in the Collateral. The SBA hereby confirms the foregoing subordination in favor of the Bank is effective regardless of the relative time of attachment or perfection of the security interest or the order of filing of financing statements or other security documents or anything in the security agreement or other credit documents executed in connection therewith to the contrary.

Postponement of Enforcement Rights by the SBA. So long as any obligation of the Debtor to the Bank secured by the Collateral shall remain unsatisfied, SBA will not take any action to realize on, repossess or otherwise foreclose upon any of the Collateral, including contacting or attempting to collect from the Debtor's accounts, without Bank's prior written consent. In the event SBA receives any payment in violation of this agreement, from any liquidation, disposition or sale, such payment shall first be delivered to the Bank in satisfaction and to the extent of the indebtedness of the Debtor to the Bank outstanding in respect of the Bank Credit Facilities.

Non-Contest of this Agreement. The SBA agrees that it will not at any time contest the validity or enforceability of the terms of this Agreement (including, without limitation, the Bank's senior, prior security interest and lien in the Collateral).

Effectiveness of Agreement. This Agreement shall remain in effect until written notice of its termination is given by the Bank to the SBA. This Agreement is solely for the purpose of establishing the priorities between the SBA and the Bank, and their respective successors and assigns, and no other person or persons shall have any right, benefit, priority or interest under, or because of the existence of this Agreement.

Counterpart Originals; Amendments. This Agreement may be executed in one or more counterpart originals, which taken together, shall constitute one fully executed instrument. Any signature delivered by a party by facsimile transmission or electronic means shall be deemed to be an original signature hereto. This Agreement may be amended or modified only by an instrument in writing signed by or on behalf of each of the parties hereto.

Governing Law. This Agreement shall be governed by and constructed in accordance with the laws of the State of Washington without regard to the conflicts of law principles thereof. Unless the context otherwise requires, all terms used herein which are defined in the Uniform Commercial Code shall have the meaning therein stated.

Integration. This Agreement contains the entire agreement between the SBA and the Bank with respect to the subject matter hereof and supersedes any other agreement in writing or otherwise with respect to the subject matter hereof.

Further Assurances. The SBA agrees to execute such other documents or agreements as the Bank may reasonably request from time to time in order to effectuate the purposes of this Agreement.

Notices. All notices required or permitted to be given hereunder shall be in writing and shall be hand delivered or sent by certified mail, return receipt requested, or express courier service, in all cases with postage or other charges paid by the sender, and shall be addressed as follows:

If to the Bank:

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

If to the SBA:

U.S. Small Business Administration

\_\_\_\_\_  
\_\_\_\_\_

or to such other addresses as the addressee shall have specified by notice given in compliance with this Section. Notice shall be deemed given upon receipt by the party to whom such notice is directed.

WAIVER OF JURY TRIAL. EACH PARTY HERETO WAIVES, TO THE EXTENT PERMITTED BY APPLICABLE LAW, TRIAL BY JURY IN ANY LITIGATION IN ANY

COURT WITH RESPECT TO, IN CONNECTION WITH, OR ARISING OUT OF THIS AGREEMENT OR ANY INSTRUMENT OR DOCUMENT DELIVERED PURSUANT HERETO, OR ANY OTHER CLAIM OR DISPUTE HOWSOEVER ARISING, BETWEEN ANY OF THE PARTIES HERETO. EACH OF THE PARTIES HERETO CONFIRMS THAT THE FOREGOING WAIVERS ARE INFORMED AND FREELY MADE.

IN WITNESS WHEREOF, each party had caused this Agreement to be duly executed and delivered by its duly authorized officer as of the day and year first above written.

SBA:

BANK:

U.S. SMALL BUSINESS ADMINISTRATION

[NAME OF BANK]

By: \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

Title: \_\_\_\_\_