

Appendix H

Model Loan Processing Procedures

APPENDIX H

LOAN PROCESSING

INTRODUCTION

WHAT IS THE PURPOSE OF THIS MANUAL?

This Loan Processing Manual (Manual) stipulates the policy and procedures for the processing of all requests for financial assistance under the Agency's enterprise loan programs. This Manual also provides the text of the Regulations, which correspond to making Agency SME guaranty loans. The Regulations govern the Agency policies and procedures and are written in bold text; while the policy is written in standard text. This Manual is written to and for all Agency personnel engaged in the processing of enterprise loans, including both the recommending and approving officials.

Unless specified within the body of the rule, the regulatory requirements of the enterprise loan programs cannot be altered or waived by the Agency without publishing a notice of the change. The policy and procedures of the enterprise loan program are divided between the policies directly associated with statutory or regulatory provisions of the law or regulation and those promulgated, (established under the authority provided the Agency) to maintain both prudent and quality lending practices. Policies directly associated with law cannot be waived and regulation cannot be waived unless, through a notice procedure as stated above. The purpose of this is to restrict the Agency from providing preferential treatment to any one borrower or to a specific group of borrowers.

This Manual is to be used in conjunction with Agency training programs that provide technical support and guidance on credit analysis to be used during the processing function.

CHAPTER 1 - GENERAL PROVISIONS

1. WHICH LOAN PROGRAMS DOES THIS PART COVER?

This Part regulates the Agency's financial assistance to small and medium enterprises under its loan programs, as authorized by legislation ("the Act"), of the Peoples Republic of China.

2. DESCRIPTIONS OF THE ENTERPRISE LOAN PROGRAMS

Program loans provide financing for general enterprise purposes, and a portion of each loan made by an authorized lender, is guaranteed by the Agency.

- A. A guaranteed loan is initiated by a Lender agreeing to make an Agency guaranteed loan to a small or medium enterprise (SME). The Lender applies to the Agency for the Agency's guaranty under a blanket guaranty agreement (Participation Agreement) that is executed by the Agency and the Lender. If the Agency agrees to guaranty (authorizes) a portion of the loan, the Lender funds and services the loan. If the borrower defaults on the loan, the Agency's guaranty requires the Agency to purchase its portion of the outstanding balance, upon demand by the Lender and subject to specific conditions.
- B. The Agency has legislative authority to provide guaranty Program loans to eligible small and medium enterprises. However, the ability of the Agency to provide Program financial assistance depends upon the availability of appropriated funds that are used for program losses.
- C. Remember, a guaranteed loan by the Agency is actually a lender's loan approved and funded by a qualified cooperating lender. The Agency's guaranty is subject to the Agency's regulations and policies applicable to all Program loans.

3. DEFINITIONS USED IN THE ENTERPRISE LOAN PROGRAMS

The following terms have the same meaning wherever they are used in this part. Defined terms are capitalized wherever they appear.

Associate

- (A) An Associate of a Lender is:
 - (i) An officer, director, key employee, or holder of 20 percent or more of the value of the Lender's stock or debt instruments, or an agent involved in the loan process;

- (ii) Any entity in which one or more individuals referred to in paragraphs (1)(i) of this definition or a Close Relative of any such individual who owns or controls at least 20 percent.
- (B) An Associate of an SME is:
 - (i) An officer, director, owner of more than 20 percent of the equity, or key employee of the SME;
 - (ii) Any entity in which one or more individuals referred to above owns or controls at least 20 percent; and
- (C) For purposes of this definition, the time during which an Associate relationship exists commences six months before the following dates and continues as long as the participation agreement or loan is outstanding:
 - (i) For a Lender, the date of application for a loan guaranty on behalf of an applicant; or
 - (ii) For an SME, the date of the loan application to Lender.

Authorization

An Authorization is the Agency's written agreement providing the terms and conditions under which the Agency will make or guaranty enterprise loans. It is not a contract to make a loan.

Borrower

A Borrower is the obligor of the loan guaranteed by the Agency.

Close Relative

A Close Relative is a spouse; a parent; or a child or sibling, or the spouse of any such person.

Lender

A Lender is an institution that has executed a Participation Agreement with the Agency under the guaranteed loan program.

Guarantor

A guarantor can be an individual or an organization that agrees to pay an obligation if a borrower fails to make payment in full.

Re-Guarantor

For the purposes of this guidance, a re-guarantor is an entity at some level that agrees to back, in whole or in part; the guaranty issued by another entity or has agreed to share the risk on such guaranty.

Loan Instruments

Loan Instruments are the Authorization, note, instruments of hypothecation, and All other agreements and documents related to a loan.

Preference

Preference is any arrangement giving a Lender a preferred position compared to The Agency relating to the making, servicing, or liquidation of a enterprise loan with respect to such things as repayment, collateral, guarantees, control, maintenance of a compensating balance, purchase of a Certificate of deposit or acceptance of a separate or companion loan, without the Agency's consent.

Principal

Principal is a term that does not have a single definition. However, there is a standard definition that shall be used if no further definition is provided. The standard definition of principal includes the following: sole proprietors; general partners; limited partners owning 20 percent or more of the equity of the enterprise; and all owners of 20 percent or more of the equity of a corporation.

This definition shall be used whenever the term principal is used unless a different definition is provided.

Principal may also include corporate officers with between 5 - 20 percent ownership of a corporation, all guarantors, and other key employees. These additional entities will be added to the standard definition of principal in those instances where needed.

Principal can also mean a married couple where both own some interest in the Applicant and together they own at least 20 percent.

CHAPTER 2 - ENTERPRISE LOAN ELIGIBILITY

1. REGULATIONS AND POLICES APPLICABLE TO ALL LOANS

The regulatory requirements applicable to all enterprise loans are described in the Regulations. The policies and procedures for all enterprise loans are described in chapters 2 through 7 of this Manual.

Policies Applying to All Enterprise Loans

The following Agency eligibility requirements apply to all Agency enterprise loans. An applicant must be in compliance with the Regulations and policies of the Agency at the time of application to be eligible for financial assistance from this Agency.

A. When Should Eligibility Be Determined?

The determination of eligibility of every applicant should be made as soon as possible in the loan making process. You can often make a preliminary determination during the applicant's or the lender's first contact with the Agency. If the enterprise is complex or unique, you should recommend to the applicant or lender to request a formal eligibility determination prior to applying. You should advise the applicant or lender as soon as an application is determined to be ineligible or when eligibility problems appear likely. This prevents unnecessary expense and frustration in the preparation of the Agency application. When advising the applicant or lender about eligibility, make clear that credit has not yet been analyzed. The Satellite Office determines final eligibility based on the information provided at the time of application.

B. May Eligibility Be Considered Prior To Formal Application?

Yes. At times a case may come to the attention of the processing office before actual application is made which has eligibility questions associated with it. The Agency may accept a written request from either a lender or applicant requesting a formal eligibility determination prior to receipt of the application. The letter should be addressed to the approving official and include sufficient information for an adequate determination on the relevant eligibility factors. Counsel may be consulted as necessary.

C. Who Has Authority to Make Eligibility Determinations?

Officials with authority to take final action on the assistance requested also have the authority to make the ultimate eligibility determinations about the application. The Credit Officer generally makes a recommendation regarding

eligibility, and the approving authority takes final action. If there is a question about eligibility, like an unusual or complex situation or one without a clear precedent, the approving official must consult the Agency field counsel for a legal opinion.

If there is a difference of opinion between the Program Office and field counsel, every effort should be made to reach an accord. If one cannot be reached, each must prepare a memorandum summarizing his or her position and forward it through the Satellite Office Director or their designee. The Program Manager must consult with the Office of Legal Counsel for legal advice. If the Program Manager and Legal Counsel do not agree on the determination, they will submit the eligibility issue to the Director's designee for final decision.

2. ELIGIBILITY REQUIREMENTS FOR ENTERPRISE LOANS

To be eligible for an Agency enterprise loan, a SME applicant must:

A. Be an operating enterprise:

a. Impact of the Form of Enterprise Entity on Eligibility

Any legal form is eligible so long as it meets any eligibility requirements set out in the Law or Regulations. If the entity is a joint venture, no more than __ percent of the joint venture may be foreign enterprise entities.

b. The products and services of the SME must be available to the general public.

c. Be organized for profit.

All recipients of the Agency enterprise loan assistance must be organized For-profit or if allowed by Law, a for-profit entity owned by a non-profit or government is eligible.

d. Be located in the Peoples Republic of China and all funds borrowed must be for operations located in the PRC.

e. Meet the size requirements provided for in the Law and the Rules and Regulations. All size determinations will be calculated including all affiliates of the applicant.

f. Size Requirements

See Chapter 3 for the basic size requirements. Applicant must demonstrate a need for the desired credit.

- g. An applicant demonstrates need if it is unable to obtain the desired credit from non-Agency lending sources, i.e., banks, credit unions, SME lending companies, etc., on reasonable terms for valid enterprise purposes. An applicant must use assets owned by it or its affiliates that are not needed for the operation of the affiliated Enterprises before it may qualify for the Agency's financial assistance. A financing need exists when the desired capital is not available through the operations of the applicant or its affiliates.
- h. Applicants that have not yet commenced operation shall have their eligibility criteria based on what the enterprise intends to do rather than on what it is doing on the day of application.

Since start-ups are generally seen as entities that can have a significant impact on the creation of employment opportunities, varied incentives may be considered to help direct lending to this group.

3. THE AGENCY'S CREDIT ELSEWHERE CRITERIA

During the early phases of the National Guaranty Program, when the primary purpose is to acquaint and familiarize lenders with SME lending, the requirement that credit NOT be otherwise available on reasonable terms may be postponed until such time as the lending community has made appropriate inroads toward satisfying the credit needs of SMEs.

As an Agency that relies upon public funding to support its lending programs, the Agency cannot provide financial assistance to SMEs that have the ability to obtain the financing on reasonable terms without government assistance. Therefore the Agency has a "credit elsewhere test" to which all enterprise loan applicants are subject. Credit not available elsewhere.

The Agency provides enterprise loan assistance only to applicants for whom the desired credit is not otherwise available on reasonable terms from non-Agency sources. The Agency requires the Lender to certify or otherwise show that the desired credit is unavailable to the applicant on reasonable terms and conditions from non-Agency sources without the Agency assistance, taking into consideration the prevailing rates and terms in the community in or near where the applicant conducts enterprise, for similar purposes and periods of time. Submission of an application to the Agency by a Lender constitutes certification by the Lender that it has examined the availability of credit to the applicant, has based its certification upon that examination, and has substantiation in its file to support the certification.

- a. The Credit Elsewhere "Test":

Credit Elsewhere is an eligibility factor that must be determined prior to assessing the credit factors of a loan request. The purpose of Credit Elsewhere

is to determine if the applicant concern along with its affiliates and principals has the ability to obtain some or all of the requested loan funds from alternative sources without causing undue hardship to the applicant, its affiliate(s), or principal(s). These alternative sources include:

- (1) The lending institution;
- (2) The internal resources of the applicant concern;
- (3) The external resources of the applicant concern;
- (4) The personal resources of the principals of the applicant concern.
If the financial assistance applied for is otherwise available on reasonable terms from any of these sources, the application must be denied.

b. The Lending Institution as an Alternative Source:

Lending institutions are a source of credit for SMEs. If a lending institution will provide the credit to the SME applicant, on reasonable terms, without the Agency support, the requested financing is not eligible for the Agency consideration. As part of the Credit Elsewhere Test, every lender who applies to the Agency for a guaranty of a loan they propose to make to a SME must signify that they could not make the proposed loan without the Agency support. Lenders have to substantiate their compliance with the credit elsewhere Regulations.

c. Lender Substantiation of Compliance with Credit Elsewhere

Third-party lenders and Program lenders must explain to the Agency the factors that prevent the financing from being accomplished without the Agency support. The lender must retain the explanation in the applicant's file.

d. What Factors Are Acceptable as Substantiation?

Acceptable factors are those that demonstrate an identifiable weakness in the credit or exceed policy limits of the lender. These factors include, among others:

- (1) The enterprise needs a longer maturity than the lender's policy permits (for example, the enterprise needs a loan that is not on a demand basis);
- (2) The requested loan exceeds either the lender's legal limit or policy limit regarding the amount that it can loan to one customer;

- (3) The lender's liquidity depends upon selling the guaranteed portion of the loan on the secondary market;
- (4) The collateral does not meet the lender's policy requirements because of its uniqueness or low value;
- (5) The lender's policy normally does not allow loans to new ventures or Enterprises in the applicant's industry; and/or
- (6) Any other factors relating to the credit that, in the lender's opinion, cannot be overcome except for the guaranty.

e. What Factors Are Not Acceptable Substantiation?

Any factors related solely to a lender's choice to obtain a guaranty without any identifiable weakness in the credit or failure of the credit to meet the lender's established policies or regulatory restrictions is unacceptable.

Unacceptable reasons:

- (1) Improve the lender's collateral lien position, or
- (2) Refinance debt already on reasonable terms.

f. What is the Certification Process Under Credit Elsewhere?

For Program loans, the lender certifies that credit is not otherwise available by signing the application form.

g. Must Consideration of Prevailing Rates and Terms Be Documented?

No, the Agency assumes the lender has considered the prevailing rates and term in its market. Just because the lender knows what may be available on an isolated basis does not require a referral of the credit to another lender.

h. The Importance of Providing Credit on Reasonable Terms.

All debt guaranteed by the Agency is on reasonable terms when made. Lenders certify this when they request the Agency to guaranty the loan they propose to make to their applicant. The Agency does not refinance debt that is already on reasonable terms. Therefore, it is important to understand how the Agency determines if a debt's terms and conditions are reasonable or why they are no longer reasonable in order to confirm that the lender's certification was correct and to know whether one of the refinancing eligibility factors has been satisfied.

i. Guidelines to Determine if Credit Terms Are Reasonable.

Generally, structuring debt in accordance with the need being financed and within the repayment ability of the borrower is reasonable and prudent financial management. We do not encourage SMEs to finance fixed asset purchases with demand notes or revolving lines of credit. We also find that loans have unreasonable credit terms if they require a debt service burden that is in excess of debt service ability. Another reason existing terms can be deemed unreasonable is when they do not allow the SME the ability to accumulate equity in the assets being financed for a prolonged period of time (such as a 10 year interest only debt due in full at maturity) or when the loan is clearly for the benefit of an individual (such as a seller taking back note that is amortized over 35 years).

j. How is the Availability of Credit on Reasonable Terms Determined?

When evaluating whether loans available from non-Agency sources are on reasonable terms, consider if the loan amounts, interest rates, maturities, payment schedules, and loan conditions from these sources can be reasonably accommodated from the cash flow of the SME. Although an SME may be able to obtain a loan from a non-Agency source, the terms or conditions may not meet its needs, and therefore be classified as unreasonable.

If the enterprise is unable to get financial assistance from non-Agency sources on terms and conditions that meets its enterprise needs, the Agency has determined that the desired credit is deemed to be not available on reasonable terms.

k. Are Balloon Notes Considered Reasonable?

No. Many Enterprises find the stability provided by fully amortized long-term debt preferable to shorter maturities with a long amortization, (balloon notes), even though interest rates may be lower on the latter. However, if the only alternative offered to guarantying a short-term loan for a long-term purpose is to guaranty a balloon note, the latter is generally of greater benefit to the SME than to accept the loan with a short-term maturity.

l. Are Demand Notes Considered Reasonable?

No. Demand notes put an enterprise in a position where its debt financing is uncertain and is at the discretion of the lender. If the note is called, which may occur for any reason, the enterprise may not be able to obtain other financing. This unduly jeopardizes the continued existence of the enterprise.

4. UTILIZATION OF PERSONAL RESOURCES

As part of its credit elsewhere test, the Agency requires that the personal assets of all owners of 20 percent or more of the applicant firm be reviewed and subject to injection in lieu of loan proceeds. This regulation is commonly known as the "utilization of personal resources test." Funds not available from alternative sources, including personal resources of principals. Policy applicable to the "utilization of personal resources test" follows.

a. What is the Purpose of the Personal Resources Rule?

Utilization of personal resources is a matter of eligibility for the Program and is required by authorizing legislation. The purpose is to restrict the use of Government-backed funding, when that funding, or a portion of it, is available from the personal resources of those individuals who stand to benefit most from the funding.

An applicant for an enterprise loan must show that the desired funds are not available from the personal resources of any owner of 20 percent or more of the equity of the applicant. The Agency will require the use of personal resources from any such owner as an injection to reduce the Agency funded portion of the total financing.

b. To Whom Does Personal Resource Rule Apply?

The Rule applies to each person that is at least a 20 percent owner as a matter of eligibility. The rule also applies to each person who owns less than 20 percent when that person is married to another owner and/or has dependent children who are owners when the combined ownership of the spouses and/or dependent children is 20 percent or more. The utilization of the personal resources rule does not apply to the enterprise resources of an associate or affiliated enterprise.

5. INELIGIBLE TYPES OF ENTERPRISES FOR ENTERPRISE LOANS

Most SMEs are eligible for financial assistance under the Agency's guaranty program. As policy direction is refined, varied incentives may be considered to help direct lending to preferred groups, such as high and new tech, labor-intensive, start-ups, and similar SMEs that public policy wants to encourage.

What Enterprises are ineligible for the Agency enterprise loans?

By statutory provisions in the Act, regulatory provisions in the Regulations and policy, some types of Enterprises are not eligible to receive enterprise loan assistance from the Agency.

How Does the Agency Determine Whether an Enterprise is Ineligible by Its Type of Enterprise?

First, decide the primary enterprise activity of the applicant. This is normally based on what the SME sells and to whom it sells it. For example, it may be a retail, manufacturing, wholesale or service enterprise. Second, determine whether it is one of the types of enterprise deemed ineligible by the Agency regulations and policy. The Agency may not make a loan to a SME for the benefit of an ineligible affiliated enterprise.

The following types of Enterprises are ineligible:

The Agency may not provide financial assistance to any SME engaged in the following activities:

- a. Non-Profit Enterprises
- b. Enterprises engaged in lending financial enterprises primarily engaged in the enterprise of lending, such as banks and finance companies.
- c. Passive holder of real and/or personal property passive enterprises owned by developers and landlords that do not actively use or occupy the assets acquired or improved with the loan proceeds.
- d. Life insurance companies; Life insurance companies are not eligible because they are actively engaged in the enterprise of investing. They invest their premium income to maintain a predictable, ready contingent cash reserve.
- e. Enterprise located in a foreign country or owned by aliens located in a foreign country. However, SMEs located in the PRC but having enterprise operations in other countries may be eligible.
- f. Illegal enterprises; enterprises engaged in any illegal activity;
- g. Enterprises, which restrict patronage; private clubs and enterprises that limit the number of memberships for reasons other than capacity;
- h. Enterprises owned by persons of poor character; enterprises with an Associate who is incarcerated, on probation, on parole, or has been indicted for a crime;
- i. Equity interest by lender or Associates in applicant concern; Enterprises in which the Lender or, or any of its Associates owns an equity interest;

6. ELIGIBLE USES FOR ENTERPRISE LOAN PROCEEDS

What are eligible uses of proceeds?

An SME must use the Agency enterprise loan for sound enterprise purposes. The use of proceeds is prescribed in each loan's Authorization.

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

- (1) Acquire land (by purchase or lease);
- (2) Improve a site (e.g., grading, streets, parking lots, landscaping)
- (3) Purchase one or more existing buildings;
- (4) Convert, expand or renovate one or more existing buildings;
- (5) Construct one or more new buildings;
- (6) Acquire (by purchase or lease) and install fixed assets

(b) A Borrower may use loan proceeds for:

- (1) Inventory;
- (2) Supplies,
- (3) Raw materials,
- (4) Working capital, and

(c) A Borrower may also use Program loan proceeds for refinancing certain outstanding debts.

7. ENTERPRISE LOAN PROCEEDS RESTRICTIONS

(a) Restrictions on uses of proceeds:

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

- Payments, distributions or loans to Associates of the applicant (except for ordinary compensation for services rendered),

- The Agency's loan proceeds cannot be used to make payment to any associate of the borrower other than to reimburse the associate for services actually rendered, and then, at a fair and reasonable rate,
- Floor plan financing or other revolving line credit; the Agency loan proceeds cannot be used for floor plan financing or any other revolving line credit,
- Investments in real or personal property acquired and held primarily for sale, lease, or investment,
- Purchase of shares of stock in a corporation to experience an appreciation in their value is an ineligible use of loan proceeds,
- A purpose that does not benefit the SME; the Agency supported loan proceeds can only be used to benefit the SME borrower. This provision restricts proceeds going to the owner(s) of an applicant concern, or
- A loan made to more than one SME, even if all of the proceeds do not benefit each enterprise, is eligible if:
 - (1) All of the proceeds benefit at least one of the SMEs;
 - (2) Each SME individually meets eligibility requirements; and,
 - (3) All of the SMEs concerned are jointly and severally liable for the loan.

(b) Payment of Delinquent Taxes

Loan proceeds must not be used to pay delinquent withholding taxes, sales taxes or similar funds held in trust since the Agency would be replacing funds that were unlawfully converted. We may consider payment of delinquent income taxes, on a case-by-case basis the same as other delinquent accounts. However, the willful failure of principals to pay income taxes is a character issue for consideration.

(c) Change Of Ownership Consideration.

Generally, it would not be recommended to provide financing for the purchase of a part of the ownership interest of an existing owner, since such a financing would offer little basis for any significant improvement to the operation of the business. However, if the transfer of business activity from the State to private ownership is identified as a key objective of the Program; parameters to finance an orderly divestiture of a SOE ownership interest may be considered.

- (1) Arm's-Length Transaction; Loan proceeds may only be used to effect a change of ownership that is an arm's-length transaction. A transaction is at arm's length if it is a reasonable representation of the fair market value, the price that an independent buyer would be willing to pay. The seller should receive no other benefit than the funds obtained from the sale, including interest in the event there is seller financing and the purchaser should receive no other benefit than the right to own and operate the enterprise and receive a profit commensurate with this operation.
- (2) Analysis of Value; to determine whether the change of ownership qualifies as arm's-length, a determination of the value of what is being acquired must be performed. When the change of ownership involves the acquisition of a going concern, the determination must be based on the reasonable expectation that the enterprise will indeed be able to continue to operate as it had in the past.
- (3) Reasons for The Sale; the loan analysis should clearly explain the reasons for the sale. Is it to permit the current owner to retire or leave because of poor health? Is it really to avoid something adverse such as a new competitor about to open or highway construction that will severely restrict access to the enterprise? Careful analysis of the financial statements needs to be conducted. Note any trends and consider local conditions. Is the area growing or decaying? Is the buyer presently an employee of the firm who already knows the market or is the buyer an inexperienced newcomer?
- (4) Documentation for a Change in Ownership Case; In order to process a change of ownership application, the proposed instruments of conveyance (generally the buy/sell agreement) must be present and they must be analyzed. The pro forma balance sheet shall be prepared to reflect what the enterprise will look like on the date ownership transfer occurs. The selling price must be compared to the value of the enterprise after the value has been determined from an independent third party. Said valuation must be obtained prior to approval or disbursement. The fact that the purchasing and selling parties have agreed to a selling price is not adequate justification that the enterprise is worth that much. The price must be substantiated by recognized methods of value determination. Financial statements of the enterprise or division being purchased are required whenever the demonstration of repayment is based in part or in full upon the historical performance of this enterprise, regardless of how the actual change of ownership will be accomplished. Consult with legal counsel whenever there are complex questions associated with any application involving a change of ownership situation.

- (5) Acquire A Going Concern; When a change of ownership involves the acquisition of a going concern, the applicant's repayment ability will be based, at least in part, on the historical performance of the former company, regardless of whether the actual change is accomplished via a stock purchase or asset purchase. When repayment is based on the historical performance of the whole company, enterprise operation, or the collection of assets acquired with loan proceeds, the historical financial statements from the seller, for no less than the last 3 complete fiscal years plus interim statements, which are no older than 90 days from receipt of application, will be required.
- (6) Acquire Assets; When a change of ownership involves the acquisition of another enterprise' assets without affecting a change in the operation status of the selling enterprise and the repayment ability of the loan will be based in full on the performance (historical and/or projected) of the buyer, rather than in any part on the historical performance of the seller, the need to obtain or verify the seller's historical financial statements is not necessary. The value of the assets needs to be substantiated. Therefore, a valuation conducted by an independent third party must be obtained prior to approval or prior to disbursement.

Note: When the purpose of the loan is to acquire the assets of another enterprise and repayment will not be based on how well these assets performed for the seller, the historical financial statements of the enterprise that is selling the assets do not have to be part of the application submission.

8. POLICIES REGARDING DEBT REFINANCING

While the refinancing of debt already incurred can frequently be problematic, it can also provide real and significant improvement to the cash flow of a business when the refinancing is for a longer period of time than that of the original loan. Such a refinancing is particularly beneficial when the original loan was made for the purpose of acquiring loan-term assets, but where the original loan was for a short-term maturity.

a. Refinancing Existing Debt

Program proceeds may be used to refinance existing debt, whether private or institutional, including credit card debt related to the enterprise. Proceeds cannot be used for general refinancing but can be used to term out debt obtained in anticipation of the project, which would have been eligible for initial financing. To be eligible for refinancing with Program proceeds, the existing debt must not presently be on reasonable terms and the refinancing must provide a substantial benefit to the SME. In addition the Agency cannot approve a loan that would pay a

creditor in a position to sustain a loss, thereby causing a shift to the Agency of all or part of a potential loss from an existing debt if the Agency would assume all or part of that same position. To be eligible for refinancing with Program proceeds, the existing debt, regardless of who the lender is or whether the debt is guaranteed, must not presently be on reasonable terms AND the refinancing must provide a substantial benefit to the SME. For purposes of refinancing, an analysis of both the reasonableness of the terms of the existing debt as well as the existing capability of the company to meet those terms at the time of refinancing must be performed. The principle test for how reasonable the terms of the existing debt are is whether the existing cash flow is adequate to meet these obligations. If a company is found to have obtained credit on reasonable terms, but is now unable to meet those terms, it may technically be eligible for refinancing. However, its inability to meet terms that once were reasonable would generally indicate a serious credit risk.

b. Analysis Considerations When Refinancing is requested

- (1) Why was the debt incurred?
- (2) Has over-obligated or imprudent debt scheduling necessitated a major restructuring of the debt?
- (3) Is the present debt already on reasonable terms?
- (4) How will the new loan improve the financial condition of the firm?
- (5) What benefit will the refinancing give to the applicant?
- (6) Does the refunding include payments to creditors in a position to sustain a loss due to either an inadequate collateral position or low or deficit net worth?
- (7) Would the Agency be likely to sustain part or all of the same loss by refinancing the debt or will additional collateral or altered terms protect the interest of the Agency?
- (8) What portion of the total loan does the refinancing constitute?
- (9) If credit card debt, for what enterprise purpose was the credit card debt incurred?

c. When May We Refinance a Participant's Debt?

The Agency may consider refinancing a cooperating lender's debt as well as the debt(s) of another lender. When a lender seeks to have the Agency proceeds used to refinance their own debt, the following additional requirements apply.

- (1) The lender must certify in writing that its debt to be refinanced is, and has been, current for at least the last 36 months. Current means that a required payment has not remained unpaid for more than 29 days. A loan that includes a payment unpaid for 30 days, subsequently deferred, was not current on that 30th day and is not eligible for refinancing. Similarly, a loan that has matured and not been paid within 29 days of the maturity date is not current and is not eligible for refinancing. A debt may be eligible for refinancing if we receive the guaranty request before the loan is 30 days past due or if the lender approved a deferment of payment for the loan before it was 30 days past due. If a lender wants to refinance debt that has not always been current, approval of the Program Manager or designee is required.
 - (2) The lender must provide a transcript of the borrower's account with the application showing that the loan to be refinanced is current and has been current for at least the last 36 months.
 - (3) When a major part of the loan proceeds is for debt repayment, the lender must fully explain how and why the debt accumulated.
 - (4) Exercise caution and prudent judgment when a loan is for 100 percent refinancing of participant debt. Provide a full justification in the file.
- d. Paying Off Seller Debt is Not Refinancing to Effect a Change of Ownership; The Agency does not classify the act of a seller using the funds they receive from a purchaser to pay off some or all of the existing debt of the seller's enterprise as refinancing, providing the purchaser is financing a complete change of ownership. A loan for this purpose is considered to be for the purchase of an enterprise, not the refinancing of any existing debts.

9. ETHICAL REQUIREMENTS PLACED ON A LENDER

The foundation of policy related to ethical requirements lies in the principle that each party to a transaction has its own interests to protect and that each party must be free to execute the transaction in a way as to protect those interests. Undue influence by another party must not be present. Each party must consummate the transaction on the basis of fair, independent analysis, as it understands its interests.

What ethical requirements apply to cooperative lenders?

Lenders must act ethically and exhibit good character. Ethical indiscretion of an Associate of a Participant will be attributed to the Participant. A Participant must promptly notify the Agency 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; take any action that will create an advantage for the lender at the expense or disadvantage of the Agency.

- (B) Have a real or apparent conflict of interest with a SME with which it is dealing (including any of its Associates or an Associate's Close Relatives) or the Agency. Conflicts of Interest or the appearance of conflicts of interest involving a participant or its associate(s) and a SME or its associate(s) must be avoided. You should also be aware that conflicts of interest or the appearance of conflicts of interest among the Agency employees, participants and applicants may exist and must also be avoided.
 - (1) Circumstances that Preclude the Agency Loans Exercise care and judgment in determining whether a conflict of interest exists. Document the file in detail. The Agency will not guaranty a loan if the participant, its associate, or a close relative or a partner:
 - (a) Has a significant direct or indirect financial or other interest in the applicant;
 - (b) Had such interest within 6 months prior to the date of application; or
 - (c) Acquires such interest at any time thereafter while the loan is outstanding.

A significant interest is one that may result in preferential treatment by the lender or the loss of independent, impartial, objective judgment, or corrective actions or the appearance of such.

For example, in addition to the physical relationship identified above, a lender may have a financial relationship that could affect, or appear to affect, its objectivity. This financial interest may include securities, with or without voting or conversion rights or warrants.

- (2) Conflict of Interest Determinations Regarding Lenders and Enterprises
The Agency may guaranty a loan if it determines that no conflict of interest exists, based on the facts of the case.

- (3) Appearance of Conflicts; The Agency employees must disqualify themselves from deciding or even participating in the consideration of a request for the Agency financial assistance when their participation raises or may raise questions of impropriety. They must do this even when no actual conflict exists if the appearance of a conflict reasonably could be perceived. Examples include, but are not limited to, the following:

- (a) Loan to a personal friend;
- (b) A loan to a former supervisor or similar person;
- (c) Where an the Agency employee is considering a enterprise or commercial transaction with an applicant or recipient of the Agency assistance; or
- (d) Where an Agency employee is involved in enterprise negotiations with an applicant or a recipient of the Agency assistance.

In cases where an "appearance" of conflict exists, official action cannot be taken by the Satellite Office until written approval is obtained from the appropriate Agency official who is responsible for Standards of Conduct issues.

- (C) Own an equity interest in a enterprise that has received or is applying to receive the Agency financing (during the term of the loan or within 6 months prior to the loan application);
- (D) Accept funding from any source that restricts, prioritizes, or conditions the types of SMEs that the Participant may assist under an the Agency program or that imposes any conditions or requirements upon recipients of the Agency assistance inconsistent with the Agency's loan programs or regulations;
- (E) Fail to disclose to the Agency all relationships between the SME and its Associates (including Close Relatives of Associates) and the Participant
- (F) Fail to disclose to the Agency 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 SME, or an Associate (including Close Relatives of Associates), to invest in the Participant;

- (G) Issue a real estate forward commitment to a builder or developer. What is a Forward Commitment? A forward commitment exists when a lender issues a commitment to a builder or developer to finance future sales of real estate. The Agency will not guaranty loans made by the lender to SMEs to purchase such real estate. This is a potential conflict of interest for the lender because of its predisposition to make the Agency loans in order to honor their prior agreement with the builder or developer. Such loans are ineligible for the Agency's guaranty regardless of whether the lender gets a fee for issuing the commitment. There have been situations where developers, brokers or lenders have created the impression that the Agency financing is readily available for new purchases in a development. The Agency and participants must be careful to avoid any perception of forward commitments. Developers and brokers should not use the availability of the Agency financing in their marketing.
- (H) Engage in any activity, which taints its objective judgment in evaluating the loan.

CHAPTER 3 – SIZE

1. SIZE STANDARDS

What are the Agency size standards?

The Agency's size standards define whether an enterprise entity is small and, thus, eligible for Government programs and preferences reserved for "SME" concerns. Size standards are established for types of economic activity, or industry.

2. ESTABLISHMENT OF AGENCY SIZE STANDARDS

How does the Agency establish size standards?

- (a) The Agency considers economic characteristics comprising the structure of an industry, including degree of competition, average firm size, start-up costs and entry barriers, and distribution of firms by size. It also considers technological changes, competition from other industries, growth trends, historical activity within an industry, unique factors occurring in the industry, which may distinguish small firms from other firms, and the objectives of its programs and the impact on those programs of different size standard levels.
- (b) As part of its review of a size standard, the Agency will investigate if any concern at or below a particular standard would be dominant in the industry. The Agency will take into consideration market share of a concern and other appropriate factors, which may allow a concern to exercise a major controlling influence on a national basis in which a number of enterprise concerns are engaged. Size standards seek to ensure that a concern that meets a specific size standard is not dominant in its field of operation.

3. AFFILIATION

What is affiliation?

- (a) General Principles of Affiliation.
 - (1) Concerns are affiliates of each other when one concern controls or has the power to control the other, or a third party or parties controls or has the power to control both.
 - (2) The Agency considers factors such as ownership, management, previous relationships with or ties to another concern, and contractual relationships, in determining whether affiliation exists.

- (3) Individuals or firms that have identical or substantially identical enterprise or economic interests, such as family members, persons with common investments, or firms that are economically dependent through contractual or other relationships, may be treated as one party with such interests aggregated.
- (4) The Agency counts the receipts or employees of the concern whose size is at issue and those of all its domestic and foreign affiliates regardless of whether the affiliates are organized for profit, in determining the concern's size.

An “affiliation” will likely exist in the case where a SOE has a significant level of ownership in the SME. At a future point in time a policy determination should be made to consider alternative measures to address this issue and should include the possibility of requiring divestiture of an SOE's ownership interests.

4. CALCULATION OF ANNUAL RECEIPTS

How does the Agency calculate annual receipts?

In determining annual receipts of a concern, “receipts” means "total income" (or in the case of a sole proprietorship, "gross income") plus the "cost of goods sold.

5. DEFINITION OF "ENTERPRISE CONCERN OR CONCERN"

How does the Agency define "enterprise concern or concern"?

- (a) A enterprise concern eligible for assistance from the Agency as a SME is a enterprise entity organized for profit, with a place of enterprise located in the Republic of China, and which operates primarily within the Republic of China or which makes a significant contribution to the Republic economy through payment of taxes or other monies.
- (b) An enterprise concern may be in the legal form of an individual proprietorship, partnership, limited liability company, corporation, joint venture, association, trust or cooperative, except that where the form is a joint venture there can be no more than 49 percent participation by foreign enterprise entities in the joint venture.
- (c) A firm will not be treated as a separate enterprise concern if a substantial portion of its assets and/or liabilities is the same as those of a predecessor entity. In such a case, the annual receipts and employees of the predecessor will be taken into account in determining size.

6. THE AGENCY'S CALCULATION OF NUMBER OF EMPLOYEES

How does the Agency calculate number of employees?

- (a) Employees counted in determining size include all individuals employed on a full-time, part-time, temporary, or other basis. The Agency will consider the totality of the circumstances, including factors relevant for tax purposes, in determining whether individuals are employees of the concern in question.

7. DETERMINATION OF A CONCERN'S "PRIMARY INDUSTRY"

How does the Agency determine a concern's "primary industry"? In determining the primary industry in which a concern or a concern combined with its affiliates is engaged, the Agency considers the distribution of receipts, employees and costs of doing enterprise among the different industries in which enterprise operations occurred for the most recently completed fiscal year. The Agency may also consider other factors, such as the distribution of patents, contract awards, and assets.

CHAPTER 4 – LOAN TERMS

1. MAXIMUM DOLLAR AMOUNTS FOR GUARANTY LOAN

- a. Total Dollar Limits On Guaranty Loans. There is no limit on the total dollar amount of an Agency loan.

As a matter of public policy, it must be determined whether available funding sources should be used to support particular segments of the SME market that would possess identifiable needs related to loan size, i.e. Should available funding help to finance many small or fewer medium-sized enterprises and should the amount of loan guaranteed be restricted to levels identified in that policy determination. Should policy direct the Program to larger SOE-owned or smaller private-owned SMEs? (See Appendix I for a variety of alternative incentives).

- b. The Agency Dollar Limits On Guaranty Loans. The maximum dollar amount of the Agency's guaranty (a/k/a the Agency share, guaranty portion, or guaranty exposure) to any one enterprise (including affiliates) either approved, committed, or in combination shall not be **more than** _____.

2. MAXIMUM PERCENTAGES OF GUARANTY FOR AGENCY LOANS

The percentage of guaranty offered on any individual loan is an excellent means of directing the Program toward its public policy purposes. The greater the guaranty, the more the loan is in keeping with the Program purposes. If a purpose is to increase financial assistance to labor intensive SMEs, the guaranty percentage on such loans might be set at a higher level than for a wholesale SME. (See Appendix I for varied alternative).

What percentage of a loan may the Agency guaranty? The Agency's guaranty percentage must not exceed the applicable percentage established in the legislation. The Agency guarantees a percentage of every loan it approves under the program. This percentage equals the Agency's pro rata share of the risk the Agency assumes on each guaranty loan. The value of the Agency's share of any approved loan equals the outstanding balance times the percentage of guaranty. The percentage remains the same through out the term of the loan, while the outstanding balance and corresponding value of the percentage guaranty declines. The maximum value the Agency guaranty can support to any one enterprise (including affiliates) cannot be more than _____.

3. MAXIMUM MATURITIES

The length of time offered a borrower to repay a loan is of great significance to a SME because the maturity determines whether the SME will be permitted to accumulate excess earnings needed to fund future needs. Frequently, SMEs suffer a disadvantage compared to larger businesses that have greater access to long-term capital. A loan guaranty can be used to help mitigate the inherently greater risk associated with longer-term financing that is often avoided by traditional lending institutions. A loan guaranty program that encourages lenders to extend maturities beyond their normal policies can be a key factor in a Program's success.

When you establish a repayment schedule and maturity, you must consider: the borrower's ability to repay, the use of proceeds, and the useful life of the assets being financed.

- (a) Establishing the maturity date.

The maturity date for an Agency loan is set in terms of the number of months from either the date of the Note or the date of initial disbursement to the date when final payment is due. A loan is not actually made until it is disbursed so maturity can be calculated from the date of first disbursement.

- (b) Who Establishes the Repayment Period?

The Agency has final approval authority for establishing the maturity period.

- (c) What limits are there on loan maturities?

The term of a loan shall be:

- (i) The shortest appropriate term, depending upon the Borrower's ability to repay. The loan maturity must be set for the shortest term in which the borrower can reasonably be expected to repay the loan. The maximum allowable maturities set forth below will not be applied if the borrower can repay the loan over a shorter period of time.
- (ii) ___ years or less, unless it finances or refinances real estate or equipment with a useful life exceeding ___ years; and
- (iii) Maturity for working capital loans. The maximum maturity for a loan for working capital is ___ years. The terms for a working capital loan should be based on the shortest period in which the borrower can repay the loan,

(iv) Maturity for non-real estate fixed assets. The maximum maturity for a loan used to purchase machinery, equipment, fixture, or furniture is ___ years, but in most cases should not exceed ___ years. When maturity exceeds ___ years for these purposes, you must document that the reasonable economic life of the item(s) acquired are greater than ___ years.

(v) Maturity for the acquisition or construction of real estate The maximum maturity for loans used to purchase existing land and buildings, finance construction of a facility expansion, and/or make significant rehabilitation of an existing structure is ___ years plus the time estimated to be reasonably necessary to complete the construction or renovation. Significant rehabilitation is defined as improvements that cost at least one-third of the purchase price or of the current appraised value of the property.

(vi) Maturity for A Loan With Mixed Purposes

When loan proceeds are used for multiple purposes (land & building, working capital, and machinery & equipment), the loan can be amortized on either a weighted average basis or by calculating the sum of equal monthly installments based on the allowable maturities of each purpose.

(vii) Limits on Maturity

The loan maturity must not exceed the period of maximum guaranty. This prohibits such structures as a working capital loan with a ___ year maturity and the Agency guaranty limited to ___ years.

A maximum of ___ years, including extensions. (A portion of a loan used to acquire or improve real property may have a term of ___ years plus an additional period needed to complete the construction or improvements.)

(viii) Maturity When Refinancing Existing Assets

The maximum maturity for a loan used to refinance either real estate or acquire fixed assets shall not exceed the remaining prudent economic life of the item(s) acquired with the proceeds of the loan being refinanced, up to ___ years. Regardless of the maturity for refinancing existing fixed assets or real property, the loan analysis must justify that the asset(s) being refinanced have an economic life not shorter than the maturity provided.

(ix) Balloon Payments

No loan that the Agency makes or guarantees can be structured with a balloon payment, unless it is documented in the file that this alternative is a significant benefit for the SME compared to any available alternative repayment structures.

4. GENERAL POLICY ON INTEREST RATES

a. General Rate Requirements for Guaranty Loans.

The maximum interest rate that may be established for any guaranty loan shall be governed by the Agency's regulations on interest rates, which shall also preempt any provisions of a state's constitution or law. The participant establishes the interest rate on guaranty loans, subject to the Agency's maximum rates, notwithstanding any Provincial law or constitutional provision to the contrary.

The basis for the Agency maximum interest rate for all guaranty loans, regardless of whether the loan is amortized on a fixed or variable rate basis, is an acceptable base rate plus allowable spread, all of which are established exclusively by the Agency. Except for variable interest rate loans, a lender must not increase the rate of interest on an the Agency guaranty loan as long as the guaranty is in effect, or increase the interest rate on the lender's share of an immediate participation loan as long as the Agency is participating in the loan.

b. Base Rate, Allowable Spread, and Allowable Variance

The base rate for all guaranteed loans depends on whether the loan is amortized on a fixed or variable rate basis. For loans amortized on a fixed rate basis, the base rate is the low prime rate, as published in a national financial newspaper each enterprise day, in effect on the date the Agency receives an acceptable application. For loans amortized on a variable rate basis, the base rate is either the same base rate used for fixed rate loans.

The allowable spread is based on the maturity of the loan. For loans with original maturities less than seven years, the maximum allowable rate cannot exceed ____ percent over the prime rate. For loans with original maturities of seven years or more, the maximum allowable rate cannot exceed ____ percent over the prime rate.

5. POLICY ON FIXED INTEREST RATES

Whether fixed or variable, the rate of interest charged on a loan is generally reflective of the degree of risk the lender has analyzed to exist in approving that loan. As a result, loans made to SMEs often carry a higher rate of interest than loans made to larger businesses with greater sources of funds to mitigate the risk of loan repayment. Arbitrary restrictions on the maximum rate a lender may charge, while often well intentioned, generally result in increased reluctance of lenders to make loans to SMEs. Great care must be exercised in formulating interest rate policy.

What fixed interest rates may a Lender charge?

From time to time the Agency will determine the maximum fixed that a lender may charge on a guaranteed loan to an SME.

6. POLICY ON VARIABLE INTEREST RATES

What conditions apply for variable interest rates?

A Lender may use a variable rate of interest, upon the Agency's approval. The Agency's maximum allowable rates apply only to the initial rate on the date the Agency received the loan application. The Agency shall approve the use of a variable interest rate under the following conditions:

- (a) Frequency. The first change may occur on the first calendar day of the month following initial disbursement, using the base rate (see paragraph (c) of this section) in effect on the first enterprise day of the month. After that, changes may occur no more often than monthly.
- (b) Range of fluctuation. The amount of fluctuation shall be equal to the movement in the base rate. The difference between the initial rate and the ceiling rate may be no greater than the difference between the initial rate and the floor rate.
- (c) Base rate. The base rate shall be the prime rate in effect on the first enterprise day of the month, printed in a national financial newspaper published each enterprise day.
- (d) Maturities under __ years. For loans with maturities under seven years, the maximum interest rate shall not exceed _____ percentage points over the base rate.

- (e) Maturities of ___ years or more. For loans with maturities of seven or more years, the maximum interest rate shall not exceed _____ percentage points over the base rate.
- (f) Amortization. Initial amortization of principal and interest may be computed and reassessed as interest rates fluctuate, as directed by the Agency. With prior approval of the Agency, the Lender may use certain other amortization methods, except that the Agency does not allow balloon payments.

7. INTEREST RATE REQUIREMENTS FOR AN AGENCY NOTE

A. Key Elements

The following elements must be included in an Agency note:

- (1) Identification of the rate being used as the base rate;
- (2) The publication in which the designated base rate appears regularly;
- (3) The lender's permanent percentage spread to be added to the base rate;
- (4) The initial interest rate of the loan (from disbursement to first adjustment);
- (5) The date of the first rate adjustment; and
- (6) The frequency of rate adjustment, or interval.

8. WHAT ARE THE LIMITS ON DISBURSEMENTS?

The disbursement period must be stated in the loan authorization and must be tailored to meet the requirements of each individual loan. The initial disbursement period should be no less than 2 months and must not be more than 3 months from the date of the authorization. An exception is permitted if the purpose of the loan is to provide permanent financing for an interim construction project, in which case the initial disbursement can be set for a time period that allows for the completion of the construction providing this time period does not exceed 12 months. The maximum final disbursement cannot be established for more than 12 months, unless the purpose is for construction or take out construction financing, in which case the final disbursement can be up to 18 months from the date of the authorization.

9. THE GUARANTY FEE POLICY FOR AGENCY LOANS

If the guaranty fee is not paid, the Agency may terminate the guaranty. The Borrower may use working capital loan proceeds to reimburse the Lender for the guaranty fee. Acceptance of the guaranty fee by the Agency shall not waive any right of the

Agency arising from the Lender's misconduct or violation of any provision of this part, the guaranty agreement, the Authorization, or other loan documents.

10. OTHER FEES ALLOWABLE BY THE AGENCY

The amounts of fees to be permitted should be considered along with any restrictions placed on interest rates. A balance must be developed and maintained that permits the lending community to offset increased costs of becoming active SME lenders, but not permitted to obtain unreasonably high or excessive returns on its loans. While it is normal for a lender to expect to profit from its loans, when considering the reasonableness of fees to be permitted, the guarantor must consider that it has minimized the lenders risk of loss by guarantying a portion of its loan and that the potential loss is one part of the lender's cost that would otherwise be covered by the fees. In other words, the lender should require less fee income to help protect against losses because the guaranty is addressing at least part of that cost.

The Lender shall also pay the Agency an annual service fee equal to ___ percent of the outstanding balance of the guaranteed portion of each loan. The service fee cannot be charged to the Borrower. The Agency may institute a late fee charge for delinquent payments of the annual service fee to cover administrative costs associated with collecting delinquent fees.

- (A) Service and packaging fees. The Lender may charge an applicant reasonable fees (customary for similar Lenders in the geographic area where the loan is being made) for packaging and other services. The Lender must advise the applicant in writing that the applicant is not required to obtain or pay for unwanted services. The applicant is responsible for deciding whether fees are reasonable. The Agency may review these fees at any time. Lender must refund any such fee considered unreasonable by the Agency.
- (B) Extraordinary servicing needs. The Lender may charge the applicant a service fee for performing servicing in addition to that is routinely required by a prudent lender.
- (C) Out-of-pocket expenses. The Lender may collect from the applicant necessary out-of-pocket expenses such as filing or recording fees. A lender may be reimbursed by the borrower for all direct cost associated with recordation of collateral instruments, and for appraisals and environmental impact reports that are obtained in compliance with the Agency policy.
- (D) Late payment fee. The Lender may charge the Borrower a late payment. A lender may impose a penalty fee of not more than ___ percent of the monthly installment amount for late payment on a loan, which the Agency guarantees.

The lender may charge this fee to a borrower who is more than ___ days delinquent on its regularly scheduled payment.

- (E) No prepayment fee. The Lender may not charge a fee for full or partial prepayment of a loan.
- (F) Other Penalties and Fees. The Agency does not allow prepayment penalty fees on loans, which it guarantees. A lender must not require an applicant to pay an application fee for filing an application or a commitment fee with respect to an approved loan.

CHAPTER 5 – CREDIT

1. THE AGENCY'S LENDING CRITERIA

One of the most critical elements in the development of a successful loan guaranty program is the establishment of standardized methods to be used in analyzing credit risk. Use of such methods consistently will greatly facilitate the monitoring of loan guaranty portfolio performance and corrective actions will be much easier to identify and implemented.

What are the Agency's lending criteria?

The applicant must be credit worthy. Loans must be so sound as to reasonably assure repayment. The Agency will consider:

(A) Character, reputation, and credit history of the borrower

Have the principals historically shown the willingness and ability to pay their debts? Have they abided by the laws of their community? While the lender will normally be more knowledgeable about the strength of a principal's character, the Credit Officer must be attentive to information contained in the credit file, which may have an impact on this issue

(B) Experience and depth of management

In assessing management ability, consider such factors as education, experience and motivation. While the opinion of the lender must be considered, you must independently assess and evaluate the applicant's management ability or potential. You may comment briefly in the loan report when management skill is clearly satisfactory. Otherwise, address any weaknesses and identify ways to improve deficient areas. You may consider requiring training or other assistance as a prerequisite to disbursement.

(C) Financial strength of the enterprise

We judge the financial strength of an enterprise by analysis and consideration of:

- (1) Balance Sheets - Understanding past operations is necessary to know where the firm is headed. Balance sheets allow you to chart the history of where a firm has been and where it is as of the current statement. The pro forma balance sheet shows you where it is headed. In analyzing the pro forma you must do the following:

- (a) Evaluate the balance sheet and make any necessary adjustments by deleting intangibles, such as goodwill not associated with the purchase of a going concern, old accounts receivable, non-enterprise assets and other items as appropriate. Note: goodwill in the purchase of a going concern may be a legitimate value, albeit a soft value, which may add support to an otherwise well-leveraged capital position.
- (b) Adjust inflated asset values and excessive depreciation and evaluate questionable items.
- (d) Perform sufficient ratio analysis to understand past operations and trends and to assure that resources are adequate for the enterprise's needs. You must also analyze the factors that make up the ratios and their impact on the financial condition of the enterprise.
- (e) Adequate working capital is of major importance to most the Agency borrowers. Many firms have failed before reaching their potential due solely to inadequate working capital. The analysis allows you to construct the relevant balance sheet components of the applicant based only on projected sales and industry averages. It reveals the dollar amount of cash, accounts receivable, inventory and accounts payable that the average firm would have at the projected sales level. Comparison to the pro forma balance sheet of the applicant allows for a direct comparison of working capital adequacy.

If necessary, as in the case for most start-ups, you may also require the applicant to provide a detailed cash flow projection. Consider increasing the loan amount if the request does not provide for sufficient working capital. Do not reduce a needed working capital portion of a loan merely to improve the debt to net worth ratio or to reduce a collateral shortage. Also, be aware of the additional costs, which might result from the Agency or lender imposed conditions.

(2) Asset Revaluation

The revaluation of assets to increase net worth occasionally has merit but often does not. Revaluations are frequently cosmetic intended simply to improve the balance sheet. Before accepting them, carefully evaluate the following:

- (a) The focus of appreciation claims is usually real estate. Other assets rarely appreciate. Revaluation may have validity if the

real estate has been held for a long period and market values have increased.

- (b) Claims of appreciation of newly purchased assets are seldom valid. The purchase price of such assets is usually a better test of value for analysis purposes
- (c) If you increase the pro forma net worth by means of asset revaluation, the entry must be justified in the loan report and supported by a written appraisal.

(3) Repayment Ability

Historical earnings and cash flow are the best bases upon which to gauge repayment ability. Projections are to be considered the basis for determining repayment when there is a change in the circumstances affecting the enterprise or a lack of historical financial data. Regardless of whether historical or projected performance is the basis for repayment, all expenses (e.g., operating expenses, owners withdrawals, salaries, dividends, etc.) must be considered when evaluating repayment ability.

(a) Historical Cash Flow

The best evidence of repayment ability is sufficient cash flow from prior operations to retire the anticipated annual fixed obligations of the enterprise. Always note any trends in revenues and cash flows. Interim operating statements may not be a reliable basis for loan approvals, particularly where the interim results are inconsistent with the prior operating results. Interim statements for seasonal Enterprises can be especially misleading.

(b) Projected Cash Flow

If historical cash flow does not demonstrate repayment ability, a realistic projection of future earnings must be used. The projections must be tested against industry averages and historical operations to assess feasibility. You must explain any significant variations.

(c) Ability to repay the loan with earnings from the enterprise;

(1) If a short-term loan, the ability to repay a loan will likely be expected to come from the conversion of the asset financed into cash, thereby creating the monies to be used for debt

payment. If the assets being financed are capital assets with useful lives of more than one year, it will generally be more appropriate to finance such purposes over a long-term period of time.

(2) If a long-term loan, the ability to repay a loan from the cash flow of the enterprise is the most important consideration in the Agency's loan making process. All the Agency loans must be of such sound value or so secured as to reasonably assure repayment. Sound value contemplates such factors as good character, earnings, collateral, management ability and financial condition. The object is not to obtain sufficient collateral to completely liquidate loans under future conditions. The Agency does not make loans based upon the liquidation value of collateral. This would be a disservice to the borrower. If you do not believe a firm can repay the loan from the cash flow of its operations, you must decline the loan application.

(d) Annual Fixed Obligations

The pro forma schedule of annual fixed obligations, which you must fully complete in the loan report, is a very important element in analyzing the ability to repay. Annual fixed obligations, including the proposed loan, are generally shown as the total principal obligation of term debt. Sometimes it may be difficult to break down an existing fixed obligation into principal and interest. You should comment in your report if interest is included as part of the fixed obligation amount.

(e) Compensation of Owners/Principals

You must consider the effect that owner compensation may have on repayment ability. Answer the following questions and any others that may be relevant.

- (i) What personal obligations and expenses does each owner have?
- (ii) How much compensation, including bonuses, perks, and benefits, is the enterprise really paying each owner?
- (iii) Are company "assets" benefiting the company or any owner?
- (iv) How do these practices impact the cash flow and repayment ability?

(v) Do the balance sheets show increases in "Loan(s) Receivable-Officer(s) or Partner(s)" accounts? Increases in these accounts usually indicate funds being paid to the officers/partners in addition to their normal compensation listed on the income statement for that year. This conceals the impact on net profits and net worth and causes the traditional rule of thumb cash flow calculation to be inflated.

(f) Actual Cash Flow vs. Rule of Thumb Cash Flow

Analysis of actual cash flow is preferred over "rule of thumb" cash flow for analyzing repayment ability. "Rule of thumb" cash flow can be distorted easily by ownership and management through their accounting practices and reporting. Net profits do not usually equate to cash available to service debt. Expenses for depreciation may be distorted as a result of management's method of allocation and may be short-term in nature. "Rule of thumb" cash flow often may indicate repayment ability when actual cash flow is insufficient or even negative. It may also incorrectly indicate an inability to repay when substantial cash flow is actually available to repay the loan. A company's actual cash flow should always be analyzed when there have been significant changes in its operations.

(g) Importance of Analyzing the Source of the Cash Flow

The presence of a positive actual cash flow is not necessarily an indication of repayment ability. If the source of the cash flow is mostly or entirely from the occurrence of debt, equity injection or sale of company assets, repayment ability may not exist.

(4) Sufficient invested equity to operate on a sound financial basis;

The Agency generally will not provide 100 percent financing for a firm. You must decide whether equity is adequate on a case-by-case basis. This is particularly important for new enterprises where a pattern of earnings has not been established. A solid equity position reduces the need for debt, provides an incentive for the principals to remain committed, provides a cushion, which helps the enterprise endure economic slumps, and improves the value of the collateral as security for the loan. Excessive debt can place unreasonable demands on a firm's ability to develop sufficient cash flows to service it.

(a) Debt to Equity Ratio

This ratio should be calculated on a tangible basis, generally discounting such soft values as organization costs, goodwill, patents, and research and development costs. Although these assets may have little or no tangible value, they may well provide an indication of strength in the enterprise. For example, goodwill may represent a realistic valuation of a company's good name and reputation when the enterprise is being sold. The debt to equity ratio varies considerably between industries making it difficult to establish a minimum acceptable ratio. However, generally you will not be able to justify approving a loan to an insolvent firm when the insolvency is due to operating losses, unless such losses were beyond the control of management.

(b) Impact of other Favorable Factors

Other favorable factors may help offset an adverse equity ratio. These could include the pledge of outside assets as collateral, the continuity of experienced management that has produced solid and consistent earnings, education and knowledge in a specialized field such as medicine or law or other factors. You may consider the value of the education of some professionals such as lawyers, doctors, and accountants to offset the lack of equity investment in terms of money or assets.

(c) Value of Assets other than Cash Injected as Equity

You must carefully evaluate the value of assets other than cash, which are injected by owners or principals because an applicant may overvalue assets either through an honest misjudgment or an attempt to embellish his or her financial investment in the new enterprise. Applicants may also undervalue their assets. Therefore, an appraisal or other valuation by a third party may be desirable.

(d) Standby Debt

Generally, standby debt from non-owners is not acceptable as the entire net worth of an applicant, especially when it occurs in new enterprise and change of ownership loans.

(e) Can Personal Debt be used for Equity Injection?

Funds borrowed through the use of personal credit for injection into the enterprise should normally be treated as debt financing, not equity injection. A lender must disclose any loan made to an individual for the purpose of providing an equity injection into the enterprise. Its loan analysis should address the impact on the personal and enterprise balance sheets and sources of repayment for such side loans. On a case-by-case basis you may be able to justify such funds as equity injection based on the analysis.

If the lender of the borrowed funds agrees to a formal standby of payment of the principal and interest until the Agency loan is paid in full, the borrowed funds may be deemed to be equity for loan purposes. The other instance in which borrowed funds may be deemed equity is if the applicant can demonstrate repayment ability from a source other than the cash flow of the enterprise or from reasonable withdrawals or salary, and excessive withdrawals or salary are not required to service the side loan. "Reasonable" withdrawals or salary means an amount comparable to that paid to someone employed to perform the same functions and duties with the same level of responsibility and authority.

(f) Impact of Debt

Simply stated, the greater the debt in comparison to the net worth, the lower the chances for success.

(D) Potential for long-term success;

Many factors affect the prospects for the survival of an enterprise. You must evaluate the financial issues, as well as many other factors. The more you know about the factors affecting the enterprise, the better you can assess the prospects and the risks.

Factors Affecting the Enterprise and the Industry are as follows:

- (1) Is the borrower in a growth, mature, or declining industry?
- (2) Does the firm have a good location for its type of enterprise?
- (3) Will local demographic factors benefit or harm the firm?
- (4) What is the Agency's experience with other enterprises in the same industry?

(5) The Agency's own experiences with loans to specific industries should be thoroughly researched and commented upon.

(E) Nature and value of collateral (although collateral will not be the sole reason for denial of a loan request

(1) It is the policy not to decline a loan where inadequacy of collateral is the only unfavorable factor. However, this does not mean that collateral is to be ignored as a credit factor, nor does it mean the analysis of collateral adequacy ends with obtaining the assets being financed or refinanced with loan proceeds. To the extent that worthwhile assets (both those financed with loan proceeds and those available from other sources) are available from either the applicants or the principals of the applicant, adequate collateral is to be required. While repayment through routine operations of the SME is the primary consideration in considering the guaranty request; it is important, nonetheless, to accurately calculate the real value of the collateral assets providing the secondary source of prepayment, as this valuation will help identify the overall level of risk associated with the loan.

The Agency loans must be secured as fully as possible with whatever worthwhile assets are available to be pledged. Collateral and personal guarantees of the principals provide a secondary means of repayment if the borrower is unable to repay the debt from its cash flow. Do not decline a loan if the only weakness in the application is the value of collateral in relation to the loan amount, provided all assets available to the enterprise and its principals have been pledged. Assets securing personal guarantees will generally be limited to those contributing the most significant collateral value such as investment real estate, residences, and occasionally investment interests.

A loan is considered fully secured if the Agency has security interests in assets with a combined "collateral" value that equals or exceeds the loan balance. For the Agency, the "Collateral" value of an asset means the amount expected to be realized if the lender took possession after a loan default and sold the asset after conducting a reasonable search for a buyer and after deducting the costs of taking possession, preserving and marketing the asset, less the value of any existing liens. Each loan analysis is to contain the market value of each asset taken as collateral and its "collateral value" using the above definition. Collateral coverage is to be based on "Collateral Value" and not market value.

When the coverage is not equal to the loan amount, the need to obtain other assets, which may be available in order to fully secure the loan, must be explored. If coverage is not full and worthwhile assets are available, they must be pledged, or the loan must be declined.

However if the loan is not fully covered and there are no additional assets to be pledged (either enterprise or personal) the loan shall not be declined solely for lack of collateral.

(2) Collateral Normally Required

(a) When loan proceeds will be used to buy assets, you must obtain a first security interest in these assets as collateral for the loan, unless otherwise justified. When the Agency refinances secured debts, we expect to have at least the same collateral as that which secured the original loan.

(b) The Agency Collateral Requirements vs. Lender's Requirements

When submitting a loan request to the Agency, the lender recommends the loan structure and various terms and conditions, including the collateral. If you disagree with the lender about any of the proposed loan conditions, including the collateral requirements, you must resolve the disagreement(s) before you recommend approval of the loan. If a lender is proposing to take collateral, which does not fully secure the loan and other collateral is available to be pledged, the Agency may decline the loan due to inadequate collateral.

(3) Assignments of Lease and Landlord's Waivers

An assignment of lease and landlord's waiver should be obtained when a substantial part of the loan proceeds are to be used for leasehold improvements or a substantial portion of the collateral consists of leasehold improvements, fixtures, machinery, or equipment that is attached to leased real estate.

(4) Value of Fixtures as Collateral

Fixtures attached to real property generally become a part of the realty. If the Agency does not have a lien on the real estate, recovery on the fixtures is unlikely. There is no problem in perfecting a lien when both the real estate and fixtures are to be taken as collateral.

(5) Current Assets as Collateral

Blanket liens on current assets such as inventory and accounts receivable generally offer little value at liquidation. Inventory is usually sold off to meet other expenses or to meet debts. Accounts receivable are hard to collect if an enterprise fails. Encumbering these assets may hurt the ability of the borrower to obtain short-term financing for seasonal needs.

(6) Insurance as Collateral

You should require life or disability insurance only to protect the Agency's interests in the event of the death or disability of a key person(s) critical to the success of the enterprise or whose continued earning power is being relied upon in making the loan. Life or disability insurance may not be necessary where the collateral is sufficient or there is adequate depth and experience of management. Coverage should be set at the minimum amount and type necessary to protect the loan. Consider the impact of the cost of the insurance (whether whole life, term, or some other form) on the working capital and cash flow. Assignment of existing insurance coverage is acceptable.

(7) Amounts in Which to Take Liens on Collateral

All liens on collateral generally must be taken/secured for the "Full" amount of the loan to protect the Government's interest or the maximum permitted by appropriate law.

CHAPTER 6 - LOAN CONDITIONS

1. BASIC LOAN CONDITIONS:

The Agency Headquarters establishes the wording for all Program and standard authorization conditions. The participant sets the terms and conditions for extending their credit. The Agency establishes the terms and conditions for its loan guaranty. The Agency must agree to any term or condition proposed by the participant lender that are not the Agency pre-approved conditions, before approval of the guaranty.

Ultimately, it is the responsibility of the Program Office to assure that the Loan Authorization has been properly developed. That responsibility may, at some point, be delegated to well-performing lenders.

A loan agreement is the document between the lender and borrower specifying the terms and conditions under which the lender agrees to provide credit. The Agency does not require that the lender to use a loan agreement.

2. PERSONAL GUARANTYS

Holders of at least a 20% ownership interest generally must guaranty the loan. The Agency, in its discretion, consulting with the Cooperating Lender, may require other appropriate individuals to guaranty the loan as well, except the Agency will not require personal guarantees from those owning less than 5% ownership. The Agency generally requires the personal guaranty of any person owning 20 percent or more of the applicant enterprise, regardless of the form of ownership.

At your discretion, you can require other appropriate individuals to guaranty a loan. For instance, when a key management person would be vital to repayment ability, you may require a guaranty, either limited or total, regardless of stock ownership. However, you must only require managers or officers of an enterprise who have no ownership interest to guaranty a loan in exceptional circumstances such as when the guaranty of the owners is weak and repayment ability is particularly dependent upon the key management person. You must also consider owners of less than 20 percent of the stock for limited or total guarantees. Whether you secure personal guaranties with liens on personal assets is a credit decision, but you should not take such action solely for the "psychological" value. Assets taken should have sufficient monetary value to qualify as worthy for collateral purposes.

A guaranty may be either secured or unsecured, but unsecured guarantees are generally of little value. All guarantors must submit financial statements in order to provide support to the evaluation of the value of each guaranty.

3. APPRAISAL REQUIREMENTS:

The Agency may require professional appraisals of the applicant's and principals' assets, a survey, or a feasibility study. For purposes of this regulation, the definition of "principal" will include the standard definition plus all guarantors. The Agency's appraisal policy pertains to the assessment of value of real estate, and the building(s) situated or to be built upon this real property.

An appraisal is a written statement independently prepared by a qualified appraiser, indicating the appraiser's opinion of the market or liquidation value of adequately described property, at a specific date, supported by the presentation of relevant market information.

A. Acceptable Appraisal Reports

To be acceptable, an appraisal must contain sufficient information to allow someone not familiar with the property to understand the basis for the determined value. An appraisal must clearly and accurately describe any extraordinary assumptions or limiting conditions that directly affect the appraisal and must indicate their impact on the value.

- (1) The Appraisal should:
 - (a) Identify and describe the real estate being appraised;
 - (b) State the real property interest being appraised, including legal description and known encumbrances;
 - (c) State the purpose and intended use of the appraisal;
 - (d) Define the value (cost, income, or comparable sales) to be estimated;
 - (e) State the dates of the appraisal and the report;
 - (f) State all assumptions and limiting conditions that affect the analysis, opinions, and conclusions;
 - (g) State the extent of the process of collecting, confirming, and reporting data;
 - (h) Describe the information considered, the procedures followed, and the reasoning that supports the analysis, opinions, and conclusion;
 - (i) Describe the appraiser's opinion of the highest and best use of the real estate, when such an opinion is necessary and appropriate;

- (j) Explain and support the exclusion of any of the usual valuation approaches;
- (k) Describe any additional information that may be appropriate and explain any departures; and
- (l) Have a signed certification by the appraiser.

4. AGENCY POLICIES REGARDING HAZARD INSURANCE:

Hazard Insurance. The Agency requires hazard insurance on all assets taken as collateral.

5. TAXES - LOAN PROCEEDS RESTRICTIONS:

Taxes. The applicant may not use any of the proceeds to pay any past-due taxes that were to have been withheld on behalf of others. Loan proceeds must not be used to repay delinquent withholding taxes, sales taxes, or similar funds held in trust, or to replenish funds used for such purpose, since the Agency would be replacing funds that were unlawfully converted. You may consider payment of delinquent income taxes on a case-by-case basis the same as other delinquent accounts. Additionally, consider whether a willful failure to pay income taxes is a character issue.

6. OTHER REQUIRED TERMS AND CONDITIONS:

A. Financial Statement Requirements

The participant shall require the borrower to submit a signed and dated balance sheet and profit & loss statement at least annually for all loans over _____. Participants can require statements more frequently on particularly large or complex loan transactions. For loans of _____ or less, the participant should require post approval financial statements of all the Agency loans to no less of a degree than on their non-the Agency loans. The standard of quality for financial statements used to process a loan will usually suffice to service the loan. You must only require audited statements when it would be imprudent to do otherwise, such as when the loan is large and is primarily collateralized with inventory or accounts receivable or both and the financial data must be of particularly good quality.

B. Flood Insurance Requirements – as appropriate.

C. Construction Loan Provision Requirements – as appropriate.

D. Special Requirements for Franchise enterprises – as appropriate.

E. Life Insurance – as appropriate.

F. Disbursement Periods

The disbursement of Program loans should occur as close to approval as is prudently possible, considering the applicant's needs for the funds and the requirements to meet the terms and conditions specified in the Authorization. As a matter of policy, the initial disbursement must occur within 6 months of approval. The only exception is when the proceeds will provide the permanent financing for an interim construction project that will take more than 6 months from approval of the Agency loan to complete.

7. ENVIRONMENTAL CONSIDERATIONS:

The Agency requires an investigation and assessment of the environmental risk on all primary collateral offered as security for any loan that the Agency is asked to guaranty in order that the risks of environmental contamination can be assessed and addressed. A lender may require its own environmental investigation of any additional collateral at its discretion.

A. What Are The Risks of Environmental Contamination?

- (1) The costs of remediation could impair the borrower's ability to repay the loan,
- (2) The value and marketability of the property could be diminished. If the borrower defaults, the Agency might have to abandon the property to avoid liability or accept a lower than expected price, and
- (3) The Agency potentially could be liable for environmental clean-up costs and third-party damage claims arising from environmental contamination if it takes title to contaminated property as a result of foreclosure proceedings or if it exercises operational control over the site.

B. Criteria for Selecting an Environmental Professional/Contractor

- (1) Environmental audits must be performed or approved by contractor personnel with adequate expertise and independence. Such expertise is evidenced by:
 - (a) A license to conduct such an audit by the government authority in which the audit will take place;
 - (b) At least ___ years experience in conducting environmental audits;

- (b) An advanced degree in engineering, environmental sciences, or geology and at least ___ years of direct experience in conducting environmental audits; or
- (c) Sufficient prior, satisfactory experience with the Program lender or first mortgage holder in conducting reliable and technically sound audits.

CHAPTER 7 - LOAN PROCESSING CONSIDERATIONS

1. REQUIREMENTS IMPOSED BY OTHER LAWS

All the Agency loans are subject to all applicable laws. The Agency requests agreements or evidence to support or document compliance with these laws.

2. IMPACT OF RULE CHANGES ON EXISTING LOANS

Regulations and contractual provisions in effect at the time of a transaction govern an Agency loan financing transaction, notwithstanding subsequent rule or contract changes. The Agency may conduct an enforcement action regarding any violation of provisions of regulations or contracts applicable at the time, but no longer in effect or in use.

3. APPLICATION FILING LOCATION

Requests for the Agency's guaranty are filed with the office location serving the area where the lender is located.

4. CONTENTS OF ENTERPRISE LOAN APPLICATIONS

The Agency requires that an application for a enterprise loan contain, among other things, a description of the history and nature of the enterprise, the amount and purpose of the loan, the collateral offered for the loan, current financial statements, historical financial statements for the past three years, and a business plan, when applicable. Personal resumes and financial statements will be required from principals of the applicant with the following:

- A. SME loan application
- B. Lender loan guaranty request
- C. SME financial statements

All Agency loan guaranty applications require financial statements on the applicant firm, including the balance sheets, reconciliation of net worth, and profit and loss statements for the 3 most recently completed fiscal years. In addition, these statements need to be current to within 90 days of the date of application. Therefore, if the most recent fiscal year end is more than 90 days from the Agency's application receipt date, interim statements have to be prepared. An enterprise that has not commenced operations is exempt from this requirement.

In addition, a debt schedule and an aging of accounts receivable and accounts payable must accompany the application. Agings are summaries of the status of the accounts rather than a detailed status of each individual account. Upon receipt of a loan package, the loan specialist shall evaluate the quality of the financial statements. You must not rely on poor quality statements (such as statements with inaccuracies or which you believe unreliable), especially when the loan request is large (more than _____).

To determine the applicant's financial condition, require that the applicant: all financial statements must be signed and dated by the proprietor, a partner, or an authorized officer of the applicant unless they are prepared by an outside accountant and properly certified. Qualified statements are not considered properly certified. It is not necessary for every page to be signed and dated.

Accurate credit analysis depends upon accurate financial statements. When the existing statements are questionable, you may require that their quality be upgraded. This upgrade can range from Compiled, Reviewed, or Audited statements, depending upon the enterprise and credit needs under review.

Note In order for you to properly analyze this data, all financial statements must be as of the same date as the balance sheet(s) used to perform the financial analysis and to develop the pro forma balance sheet.

All current financial data should be as of the same date. Additional financial data, such as earnings projections and/or cash flow statements, may be necessary for certain applications. This is especially true for new enterprises just starting or existing enterprises planning major changes in their operations. In addition, the depreciation schedule from an applicant's tax returns may be useful in determining fixed asset values.

Selected financial statements are also required from the seller of assets or an enterprise to the applicant when the analysis of repayment is dependent on how well these assets or this enterprise performed for the seller. Financial statements from the seller of assets to the applicant are not required when the analysis of repayment for the proposed loan is not dependent on historical performance.

When the applicant is acquiring assets that transfers the operation associated with the assets from the seller to the applicant, repayment will be either fully or partially be dependent on how well these assets historically performed for the seller. Under such circumstances, the financial statements (balance sheet and profit and loss) on these operations while under the control of the seller need to be included as part of the application submission. If the applicant is acquiring assets and there will be no transfer of the operation associated with the assets or enterprise, financial statements will not be required from the seller.

"Principal" in this section does not include officers with less than 5 percent ownership. Personal financial statements are required from a proprietor, each general partner, each limited partner owning 20 percent or more of an enterprise, each owner of 20 percent or more of an enterprise, each officer, and each guarantor. We may require financial statements from owners of less than 20 percent if we will require their guaranty. Since the use of personal resources may not be waived for owners of 20 percent or more of an enterprise. All personal financial statements must be signed and dated.

5. LOAN DECISION

Applicants receive notice of approval or denial by the Lender. Notice of denial will include the reasons. If a loan is approved, an Authorization will be issued.

Only those individuals with the requisite experience, training, and other qualifications as determined by the Director or designee may approve or decline loans. Depending on the personnel structure of an office, this may include non-supervisory individuals, such as team leaders. Training certification may be required in keeping with established policy.

(A) "The Rule of Two"

A loan may be approved or declined, on the basis of two concurring opinions of personnel who are appropriately trained, subject to statutory and administrative authority.

(B) Changes by the Reviewing Official

If the reviewing official changes the maturity, loan amount, or terms and conditions, the case must be treated as a split, unless both are in agreement with the change.

(C) Decisions on Splits.

Forward the application through the normal chain of command, including acting personnel when necessary, until two concurring opinions are obtained.

6. RECONSIDERATION AFTER DENIAL

An applicant may request reconsideration of a declined loan request by submitting information overcoming the stated reasons for decline within six months of the initial decline.

7. LOAN CLOSING FOR LOAN OFFICERS

A. Who Has Responsibility for Loan Closings?

The Agency counsel monitors the closing and disbursement of all loans through the final disbursement. Cooperating lenders close Agency guaranty loans. Agency counsel gives guidance to lenders on loan closing problems.

B. What Is The Credit Officer's Role in Loan Closings?

You should have a general knowledge of the Agency loan closing requirements and be able to answer procedural questions from lenders. Refer substantive or legal questions to the Agency counsel.

8. CANCELLATION AND REINSTATEMENT OF COMMITMENT

Once a loan has been guaranteed by the Agency but remains un-disbursed, it continues to have the right to cancel the guaranty for good reason. It may then also reinstate for good reason.

9. INCREASES OR ADDITIONAL LOANS

An approved loan may be increased or decreased prior to disbursement.

10. DISCLOSURE OF FEES

An Applicant for a loan must identify to the Agency the name of each Agent that helped the applicant obtain the loan, describing the services performed.