

# ARC LOAN PROGRAM

## Program Training

# Timeline

- June 8<sup>th</sup>: Regulation, Procedural Guidance and Forms Released
- Week of June 8<sup>th</sup>: Lender Training
- June 15<sup>th</sup>: SBA Begins Accepting Loans

# ARC Loan Basics

- New, temporary, guaranteed loan program
- Deferred payment loan
- Up to \$35,000
- Proceeds used to make P&I payments on qualifying small business loans (QSBL)
- Interest-free to borrower
- SBA pays interest to lender
- No fees charged by SBA or lenders to borrowers, other than direct costs of securing and liquidating collateral
- ARC Loans available until funding runs out or September 30, 2010, whichever occurs first

# ARC Loan Structure

- Disbursement Period: Up to 6 months payments of principal and interest on one or more QSBL
- Deferral Period: Loan deferred for 12 months beginning after last disbursement
- Repayment Period: Loan repaid over 5 years
- Maximum Term: 6.5 years
  - Max term will be less than 6.5 years if disbursement period is less than 6 months

- ARC loans made by 7(a) lenders
  - Delegated lenders may make ARC loans on a delegated basis if already approved to make PLP, SBA Express, Community Express and/or Patriot Express
  - Non-delegated lenders may make ARC loans by submitting them to the 7(a) Loan Guarantee Processing Center (LGPC), located at Citrus Heights, CA
  - New SBA lenders may become 7(a) lenders by following existing procedures and may make ARC loans by submitting them to the 7(a) LGPC
    - New SBA Express lenders must submit ARC Loans on a non-delegated basis
- Lenders must apply 7(a) program requirements to ARC loans unless different provisions are provided for in regulation and procedural guidance.



# Eligibility Requirements

- ARC loan borrowers must be eligible under the basic eligibility requirements for 7(a) loans including small business size standards
- Additional Requirements:
  - Viable Small Business
  - Immediate Financial Hardship



U.S. Small Business Administration

# Viabile Small Business

- Established, for-profit business
- Going concern
- Difficulty making periodic payments of principal and interest on qualifying small business loans and/or meeting operating expenses
- Able to demonstrate projected continued operation beyond the six month period of payment assistance with an ARC loan
  - Quarterly cash flow projections for the two year period after the ARC Loan is made
  - 1.0 debt service coverage acceptable (Business income covers operating/debt service expenses)



# Immediate Financial Hardship

- Lender must document and borrower must certify and provide evidence of immediate financial hardship
- An immediate financial hardship is difficulty making periodic payments of principal and interest on loans and/or difficulty meeting operating expenses based upon current business environment
- Examples include:
  - Declining sales and/or revenues;
  - Increasing expenses;
  - Reduced working capital;
  - Cash shortage due to frozen inventory or receivables, accelerated debt or reduced or frozen credit lines;
  - Difficulty in making loan payments on existing debt;
  - Difficulty in paying employees;
  - Difficulty in purchasing inventory, materials or supplies; and/or
  - Difficulty in paying rent and/or other operating expenses.

# Ineligible Small Businesses

- Ineligible small businesses for ARC loans are the same as for 7(a) loans
- Prohibited NAICS Codes:
  - Casinos
  - Casino Hotels
  - Other Gambling Industries
  - Golf Courses and Country Clubs
  - Zoos and Botanical Gardens
  - Fitness and Recreational Sports Centers
    - May be approved by 7(a) LGPC
- New Start-Up Businesses
- Business Expansions
- Previous Loss to Government

# Use of Proceeds

ONLY one eligible use of proceeds:

Making periodic payments of principal and interest on QSBLs

# Use of Proceeds

- Ineligible use of proceeds includes:
  - Any purpose other than P&I payments on QSBLs
  - Purpose that does not benefit the borrower
  - Provide or refinance funds used for payments, distributions, or loans to an associate of borrower

- Qualifying Small Business Loan: Existing Loan made to a small business concern meeting 7(a) eligibility standards
- Types of Loans:
  - Mortgages
  - Secured and unsecured loans
  - 504 first mortgages
  - Capital leases
  - Notes payable to vendors/suppliers/utilities
  - Home equity loans used to finance business operations
  - Credit card obligations
  - SBA loans made or guaranteed on or after 2/17/09 (includes 7(a), 504 and disaster loans)

- May be same institution debt and/or other institution debt
- Provisions with regard to preference and refinancing do not apply
- Lenders must consider borrowers' overall financial situation and debt burden and allocate ARC Loan proceeds in a manner designed to promote borrower's long-term viability
- Lender must document the existence of QSBL(s) and determine that the QSBL(s) are eligible for ARC proceeds

- Business Lines of Credit
  - Two forms – 6 disbursements or 1 disbursement
  - If 1 disbursement, payments on underlying LOC must be deferred for 5 months and LOC limit may not be reduced for 18 months unless underlying loan goes into non-accrual
    - Lender certifies structure is in best interest of borrower
- Home Equity Loans and Credit Card Obligations
  - May only pay for business related portion of these obligations
  - Lender must obtain documentation for each business related purpose
  - Borrowers must certify that amounts were exclusively used for business expenses
  - Payments may not exceed the amounts documented for business purposes and interest is pro-rated

# Terms and Conditions

- Maximum Size \$35,000
- 100% Guaranteed
- Interest-free to borrower
- Interest paid by SBA to lender throughout life of loan beginning with first disbursement
- Lenders may not charge default interest rates

# Terms and Conditions

- May include restructuring and deferrals of non-SBA loans as part of ARC loan transaction
- Collateral – Required consistent with conventional lending practices for similar sized commercial loans (lender certification required)
- Fees – No fees other than cost of securing and liquidating collateral
- Secondary Market – No secondary market sales and/or sales of participations

- Disbursements:
  - Directly to QSBL payee(s) (electronically or by check); and/or
  - Jointly issued checks made out to the borrower and the QSBL payee(s)
  - In no instance directly to the borrower
- Increases – only with prior written approval of SBA but total loan may not exceed \$35,000
- Personal Guarantees – required of holders of at least a 20% ownership interest
- Personal Resources Test not required

- Bankruptcy –
  - Not eligible if if not discharged or without a confirmed bankruptcy plan
  - Otherwise, may be eligible for ARC Loan based on lender’s credit analysis
- One ARC loan per small business
  - Proceeds may pay P&I on multiple QSBLs
  - Additional ARC Loan applications for affiliate businesses must be approved by 7(a) LGPC

- Lenders screen for eligibility
- Delegated lenders will complete eligibility checklist and make eligibility determinations
- Non-delegated lenders will complete eligibility checklist and submit to 7(a) LGPC

# Credit Criteria

- If borrower meets following credit criteria, delegated lenders may make ARC Loans on a delegated basis, otherwise it must be submitted to the 7(a) LGPC for approval:
  - Borrower in operation for at least 2 years
  - Annual financial statements (balance sheet, income statement, cash flows) demonstrating business is a going concern and had positive cash flow in at least one of past two years (Interim financial statements required if 90 days past borrower's fiscal year end)

# Credit Criteria

- Credit Criteria (continued)
  - Quarterly cash flow projections for two years demonstrating sufficient cash flow to meet debt burden
    - 1.0 debt service coverage is acceptable
  - Borrower certification that it is current or not more than 60 days past due on any QSBL being paid with the ARC Loan. Deferred loans are not considered past due until they have been deferred for more than 3 months.
  - Borrower certification with documentation as to immediate financial hardship
  - Acceptable business credit score (obtained by SBA)
- Loans made by non-delegated lenders must consider the same criteria but final credit decision is made at the 7(a) LGPC.

# Application of ARC Loan Disbursements

- ARC Loan payments prioritized in following order:
  - Up to six months monthly payments of scheduled principal and/or interest payments on the Borrower's QSBLs (including scheduled balloon payments)
  - Any remaining amount available on the loan in the sixth disbursement month, after the scheduled monthly principal and/or interest payments have been made, may be used to prepay principal on a QSBL

# Special Rules for Business QSBL Lines of Credit

- One single payment from an ARC Loan may be made
- Business line of credit must be same institution debt
- Underlying business line of credit must be deferred for five months subsequent to the ARC Loan disbursement
- Line of credit may not be reduced for 18 months unless loan is placed on non-accrual
- Lender must certify that such an arrangement is in the borrower's best interest (since the term of the ARC Loan will be reduced from 6 and 1/2 years to 6 years and one month)

- Delegated Lenders
  - Submit via E-Tran
  - Certify eligibility and credit criteria and submit for loan number
  - SBA obtains business credit score (Liquid Credit)
    - If loan scores within acceptable limits, loan number is provided to lender via E-Tran
    - If not within acceptable limits, loan is referred to the 7(a) LGPC for further review
- Non-Delegated Lenders
  - Lender prepares package, applies same credit criteria and submits to 7(a) LGPC for approval
  - Loan is underwritten, including a business credit score, and an approval/disapproval decision made
  - Decision communicated to lender

# Interest Payments

- Lenders calculate interest based on existing methods
- Rate of interest initially established by SBA at Prime plus 2%, adjusted on the first day of the month based on the Prime rate in effect on that date
- Lenders bill SBA for interest payable
- SBA conducts tests for reasonableness of interest payable
- If within established tolerance levels, interest payment made by SBA to lender
- SBA contractor will conduct reconciliations, audits, follow-up on lender reporting issues, and assist with overall portfolio management
- Lender agrees to make interest payment reconciling adjustments to address over and/or underpayments during life of loan

- Modeled on Express programs
- Servicing and liquidation processes same as required for non-SBA guaranteed commercial loans
- 1502 reporting basically same as for 7(a) with a few data field adjustments

- Loan Authorization Required
- Closing conditions must be satisfied before loan disbursement
- Additional closing conditions that must be met before disbursement:
  - Schedule of ARC Loan payment disbursements required
  - IRS verification of financial information
  - Third Party Payments
  - Adverse Change
  - Hazard Insurance (if collateralized)
  - Flood Insurance (if collateralized)
  - Environmental Reviews (if collateralized)
  - Child Support Payments

# Servicing Requirements

- Processes same as required for non-SBA guaranteed commercial loans
- ARC Loan deferrals allowed but loan term may not be extended so loan must be re-amortized
- Prior, written SBA consent required:
  - Increase in ARC Loan principal amount
  - Compromise principal balance or release guarantors
  - Take title to property in SBA's name
  - Take title to environmentally contaminated property
  - Transfer or pledge of a loan
  - Deferrals beyond 6 months

- Notice to SBA Required:
  - Decrease principal amount
  - Cancel loan
  - Name changes
  - Address changes
  - Loan maturity changes
  - Assumption approvals
  - Liquidation classification
  - Deferrals of 6 months or less

- Process same as required for non-SBA guaranteed commercial loans
- Liquidation
  - Lenders liquidate loans with collateral in excess of \$1,000
  - Lenders may request Treasury off-set for loans with collateral of \$1,000 or less
- Liquidation actions must be documented
- Wrap up report required upon completion of liquidation
- Application of liquidation proceeds:
  - Liquidation expenses
  - Principal balance of loan

# ARC Loan Purchases

- Not required to liquidate prior to requesting purchase
- Lenders may submit for purchase:
  - 60 days after default
  - Borrower files for bankruptcy
  - Loan involves extended liquidation issues
- SBA requires purchase no later than 120 days after earliest uncured payment default
  - No interest paid by SBA from 120 days after earliest uncured payment default
- Expedited purchase procedures to be applied
- ARC Loan purchases to be processed in Fresno and Little Rock



# Lender Portfolio Performance

- Lenders making ARC loans will have their performance assessed consistent with 7(a) and 504 practices
- Given that a higher default rate for ARC loans is expected, some accommodation will be made in performance assessment
- Lenders may be suspended or their ability to make ARC loans revoked if a lender does not continue to meet SBA program requirements

# Program Limitations

- Program level
  - Approximately \$335 MM
  - ARC Loans available until funding runs out or September 30, 2010, whichever occurs first
- Lender Limits
  - Lenders may make no more than 1,000 ARC Loans in total (no guarantee of 1,000 ARC Loans; program expires when funding is fully used or September 30, 2010, whichever occurs first)
  - Lenders may only submit 50 loans per week
  - Unused amounts may accumulate up to total of 1,000
  - Limits apply to both delegated and non-delegated loans
  - SBA will evaluate weekly limits periodically, first evaluation expected in August 2009

# Questions & Answers