



Solutions to Misunderstood Nuances of SOP 50 10 6

Wisconsin Lenders Conference
May 19, 2022

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Instructor

**Lisa Preston
President**



Curriculum

❖ Solutions to Misunderstood Nuances of SOP 50 10 6

✓ Eligibility

- 100% Ownership
- Liquidity
- Loan Structure

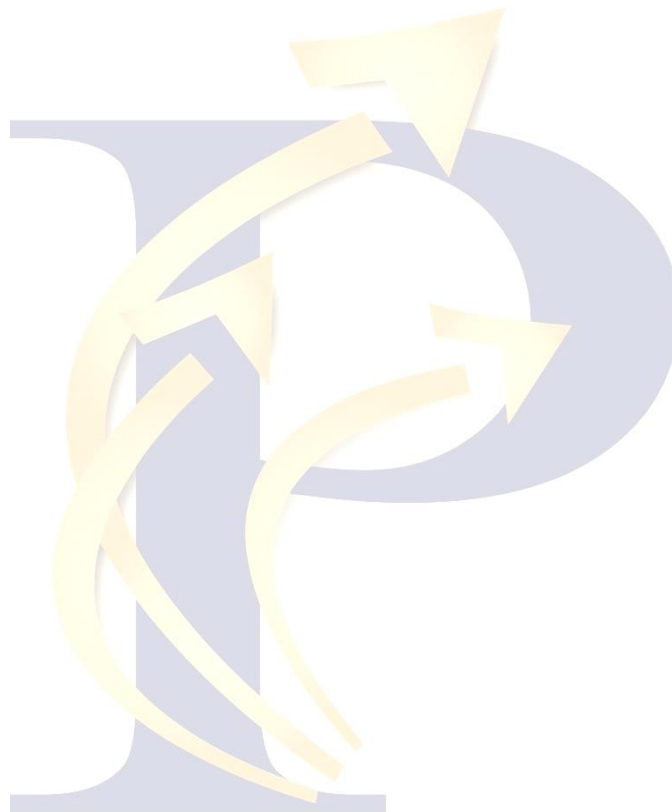


Curriculum

- ❖ **Solutions to Misunderstood Nuances of SOP 50 10 6**
 - ✓ **Underwriting**
 - **Current Economy**
 - **Working Capital**
 - ✓ **Closing**
 - **Borrower Injection**
 - ✓ **Final Thoughts**



Eligibility



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First

Eligibility

is

Eligibility

is

Eligibility!



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General Concept

- **Basic elements are same in every SBA Loan Program**
- **+ Additional requirements for Export loan programs**
- **Results are a “Go” or “No Go”**



Ownership

- **1st step in eligibility**
- **Must identify 100%**
- **Legal vs Illegal**
- **Organizational documents**
- **Consistency in documentation**
- **Document your assessment**



Know Your Borrower

- **Flowchart**
- **Business vs individual**
- **Determine % of ownership through levels of ownership**
- **Show analysis**
- **Affects:**
 - **Guarantors**



. . . Know Your Borrower

Affects:

- **Credit available elsewhere**
- **Liquidity**
- **Prior loss**
- **Affiliation / Control**
- **Outstanding SBA loan \$'s**
- **Underwriting**
- **Closing +++**



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Liquidity

- **Subset of Credit Not Available Elsewhere**
- **No actual test calculation**
- **No clear direction**
- **Subjective evaluation**
- **Business decision**



Involvement

Individual capacity assessment:

- Owners of 20% or more
- Spouse + minor children
- Knowledge of financial condition of minority interest owners
- Trust assets



... Involvement

Entity capacity assessment:

- Borrower
- Affiliates
 - Inter-company transfers
 - Involvement of operations
 - Support / Control



Liquidity Evaluation

Capacity assessment:

- **Current vs non-current assets**
- **Exclusions**
- **Use of excess funds**
- **Show analysis / How decision made in writing**



Liquidity

**Assists with
substantiating**

Credit Not Available Elsewhere!

***Discuss in Capitalization Assessment
section of Underwriting!***



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Loan Structure - Individuals

- SBA originates loans to ***small business concerns***
- SBA cannot make loans to an ***individual***
 - **Special circumstances:**
 - ✓ **Sole Proprietorship**
 - ✓ **EPC**
 - ✓ **Stock Purchase**



Loan Structure

- **Borrower**
 - **Multiple Borrowers / Co-Borrowers**
- **Eligible Passive Company / Operating Company (EPC / OC)**
 - **Co-Borrower**
 - **Guarantor**



EPC / OC

EPC – Eligible Passive Company

- Entity holds an asset and leases it to another company
- Entity must be passive and remain passive

OC – Operating Company

- Eligible small business concern leases and uses asset



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EPC / OC Format

- **Loan is issued to EPC**
- **OC must be :**
 - **Guarantor or Co-Borrower**
 - **Determine how ownership of assets held**
- **Co-Borrower if:**
 - **Any Loan Proceeds Utilized for Benefit of OC; Ex., Working Capital, Inventory, Intangible Assets, etc.**
 - **Any Loan Proceeds Will Purchase Assets Held by OC**



EPC / OC

- If loan structure correct, all other requirements fall into place
- OC must lease 100% of property from EPC; All other tenant leases must be sub-leases to OC
- Report NAICS code of OC, NOT EPC



... EPC / OC

- Only 1 EPC allowed in loan structure

Exception!

- Tenancy in common – all entities are considered 1 EPC

Must know how ownership of property held!



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Multiple Entities

- Multiple EPCs **NOT** Allowed
 - Multiple Properties within EPC **NOT** Allowed
- Multiple OCs **ARE** Allowed



Careful

- Borrower requests, lender evaluates
- Do not decide or dictate to borrower loan structure
- Only provide SBA requirements
- Borrower must choose business entity structure including loan structure

Do not create potential Lender Liability!

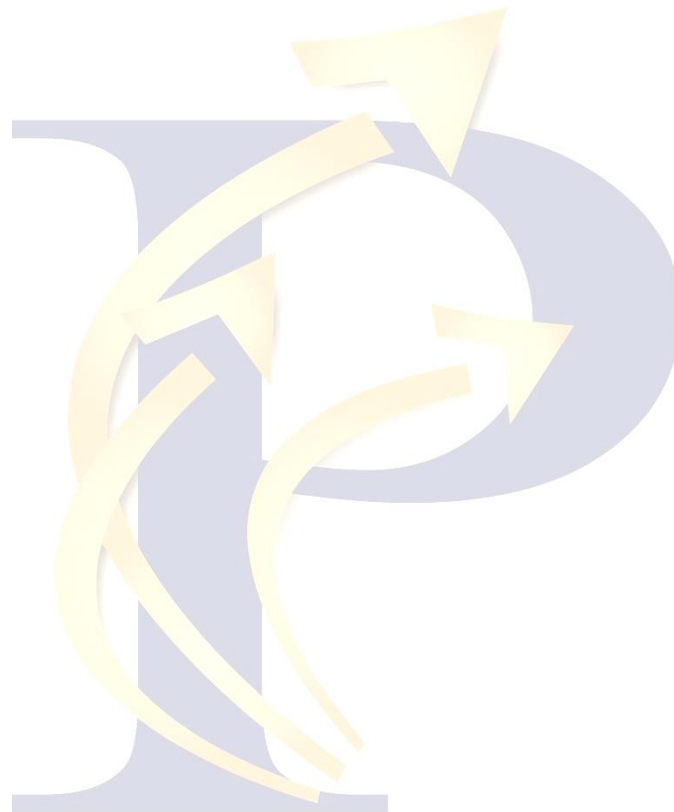


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Underwriting



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Present Economy

Narratively discuss / substantiate:

- **Borrower operations prior to pandemic**
- **Effect pandemic had on business during 2020 and 2021**
- **How business, if applicable, pivoted during pandemic**
- **If and how product / service is still needed post pandemic**



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. . . Present Economy

- **Any changes to business model**
- **Management capability / knowledge / passion**
- **Borrower's use of other programs, i.e. PPP, EIDL, etc. and present status of each loan**
- **Use interims / projections to counter negative affects of pandemic**



. . . Present Economy

- Risk mitigation factors
- Deduce & document it all
- You must **Know Your Business** in order to complete thoroughly
- If guaranty requested, SBA will judge on intent and knowledge at time of underwriting

Complete on-going viability assessment!

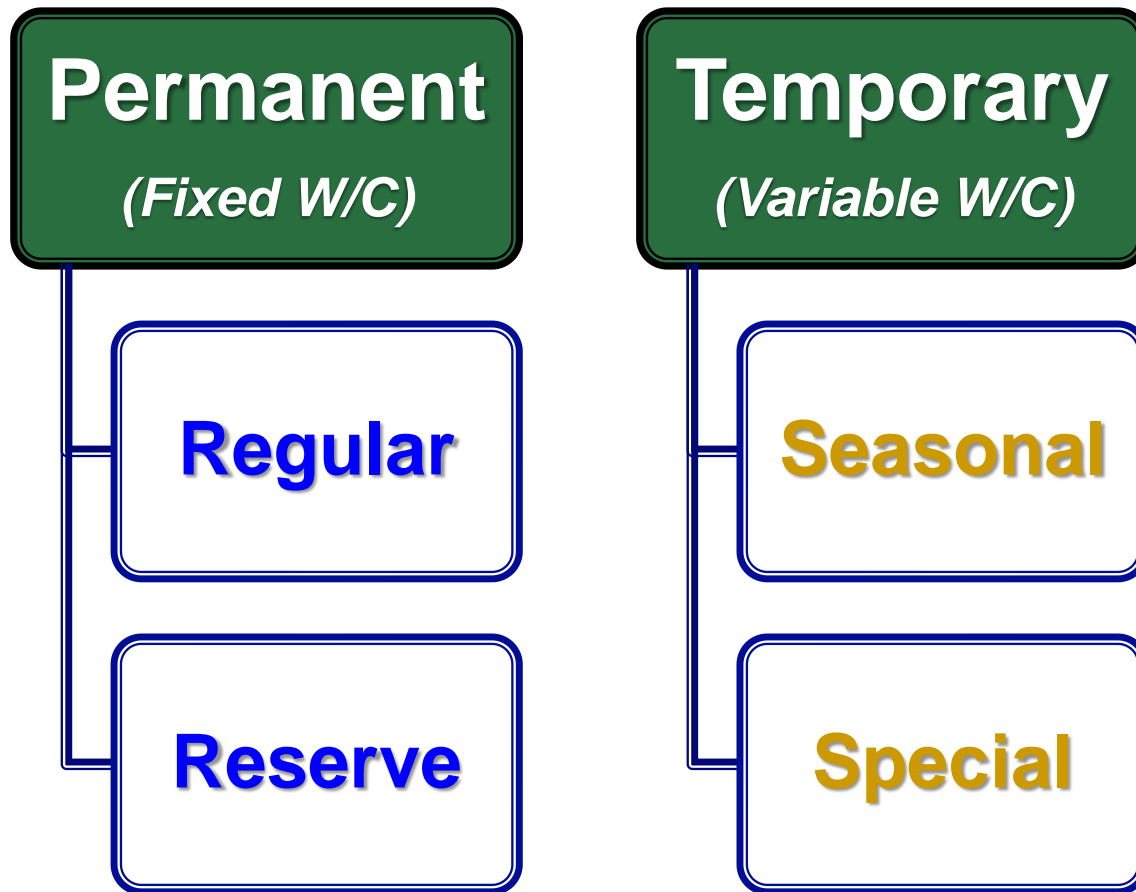


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Working Capital “Time” Need



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Permanent W/C

- **Permanent Working Capital supports foundational elements of borrower through continual life cycle of product / service offered**



Permanent “Regular” W/C

- **Least amount of \$’s business needs to fund day-to-day operations**

Examples:

- **Salaries / Wages / Contractors**
- **Overhead expenses such as, rent, utilities, insurances, office expenses, etc.**



Permanent “Reserve” W/C

- **Capital needed for unforeseen circumstances**

Examples:

- **Strikes**
- **Fires**
- **Other natural calamities**



Temporary W/C

- **Temporary Working Capital is utilized by borrowers for situational instances of varying intervals exceeding Permanent Working Capital capacity and/or Reserves**



Temporary “Seasonal” W/C

- **Capital needed during peak seasons of year or if product / service of business is seasonal by nature**

Examples:

- **Christmas or other holiday products / sales elevated**
- **Summer vs Winter sales**



Temporary “Special” W/C

- **Supplementary to other forms used for exceptional operations or unforeseen circumstances**

Examples:

- **Marketing campaigns**
- **Accidental fires**
- **Other natural calamities**



Facilities of W/C Loans

Temporary

(Revolving Line of Credit)

vs.

Permanent

(Term Loan)



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Credit Memorandum

Must identify & narratively explain:

- **Reason / need for working capital request**
- **Determine if permanent vs temporary**
- **Analyze and calculate amount of working capital need**
- **Show your analysis**



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SOP... pg. 249 & 250

- ***“Working capital adequacy for next 12 months, at a minimum” (may need to be longer)***
- ***“When 50 percent or more of the loan proceeds will be used for working capital, Lender must explain in its credit memorandum why this level of working capital is necessary and appropriate for the subject business”***



Multiple Ways to Calculate W/C

Methods:

- **Percentage of Sales**
- **Operating Cycle**
- **Regression Analysis**
- **Cash Forecasting**
- **Projected Balance Sheet**
- **Adjusted Profit / Loss**

What is your method / policy?



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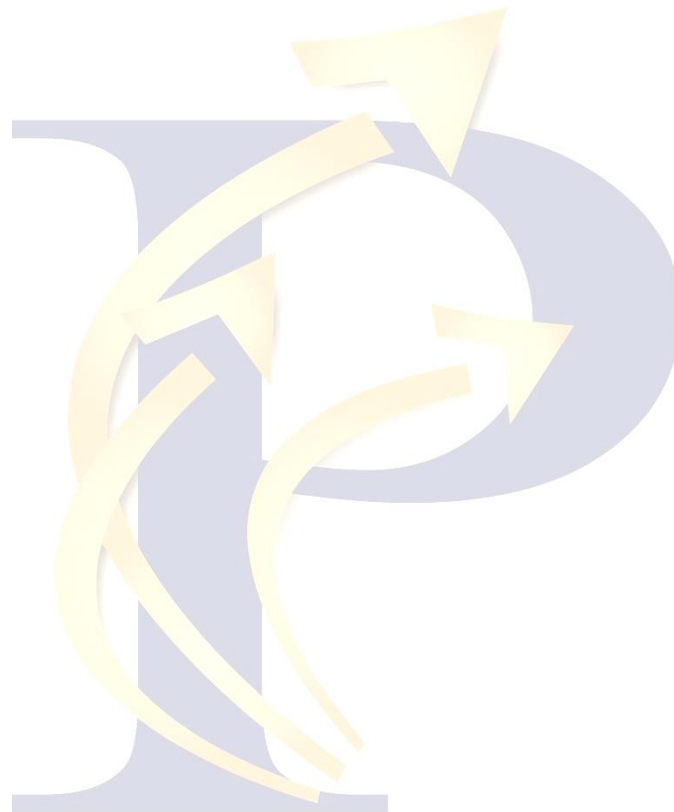
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W/C Common Issues

- **Inadequate justification**
 - **Need**
 - **Why**
 - **When**
- **Misuse for other purposes, such as debt refinancing**
- **Purchasing current or long-term assets without securing lien**



Closing



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Borrower Injection

- **Attend next session to learn about Borrower Injection**

“Got Your Authorization, Now What?”



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Final Thoughts



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Tasks to Approve

What you know:

- **Disclose**
- **Evaluate**
- **Clarify**
- **Substantiate**



Process

- **Should be methodical to:**
 - **Create efficiency**
 - **Increase profitability**
 - **Reach ultimate goal of obtaining SBA guaranty**

Anything less is not winning!



Absolute Necessity

- **Stay informed**
- **Talk to peers**
- **Teamwork**
- **Show your assessment**
- **Document, Document, Document**



Don't Forget

Be Confident . . .

Perform appropriate amount of
due diligence

Preparation and Knowledge
means Success!



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Questions



Thank You!

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