

TO: State Directors, Rural Development
ATTN: Business Programs Directors
SUBJECT: Business and Industry Guaranteed Loan Program
Clarification of Loan Processing Issues

PURPOSE/INTENDED OUTCOME:

The purpose of this Administrative Notice (AN) is to clarify several loan processing issues, including collateral coverage, equity, and preapplication requests.

COMPARISON WITH PREVIOUS AN:

This Administrative Notice (AN) replaces RD AN No. 4279 (4279-B) dated May 23, 2007.

IMPLEMENTATION RESPONSIBILITIES:

Office of Management and Budget Circular A-129 states, in part, that financing should be limited by not offering terms (including the financing of closing costs) that result in a loan-to-value equal to or greater than 100 percent. RD Instruction 4279-B, section 4279.131(b), requires a loan-to-discounted (or loan to net market) value not to exceed 100 percent, except as outlined in section 4279.131(b)(2). Section 4279.131(b)(2) allows loan-to-value (or loan to market value) coverage to be discounted accordingly for those businesses with a documented successful financial history where cashflow and profitability are strong, but under no circumstances should the loan-to-value (loan to market value) ever be equal to or greater than 100 percent. It is expected that the business must have been profitable in all of the years for which we have historical financial statements in order to be considered successful.

EXPIRATION DATE:
June 30, 2009

FILING INSTRUCTIONS:
Preceding RD Instruction 4279-B

The Agency has taken the position that real estate appraisals are required when the value of the collateral exceeds \$100,000. Chattels are evaluated in accordance with normal banking practices and generally accepted methods of determining value. Equipment is typically valued by its cost (if newly acquired) or an appraisal that establishes a fair market value, while the value of inventory and receivables is typically the book value of these assets on the balance sheet.

RD Instruction 4279-B, section 4279.131(d), requires a minimum of 10 percent tangible balance sheet equity for existing businesses and 20 percent for new businesses. A reduction in the equity requirement may be granted by the Administrator if collateralized personal and corporate guarantees are taken and pro forma and historical financial statements of the business show that it meets or exceeds the industry median quartile ratios. The loan approval official, within his/her delegated authority, may require equity in excess of the regulatory minimum in cases where there is justification to do so; however, you are cautioned to be consistent in documenting the reasoning for requiring more than the regulatory minimum equity.

In situations where a real estate holding company and an operating entity are dependent upon one another's operations and are effectively one business, you should require them to be co-borrowers, especially when you consider collateral, equity, and repayment ability. Only in situations when real estate holding companies and operating entities are truly independent and not reliant on the other's operation to survive should you allow one entity or the other to be a sole borrower. In co-borrower situations, financial statements should be presented for both borrowers individually as well as on a consolidated basis. Consolidated pro forma financial statements should be used to determine whether the equity requirement is projected to be met at loan closing.

In accordance with RD Instruction 4279-B, section 4279.119(a)(1)(iv), only preapplications in excess of \$10 million must be submitted to the National Office. Requests submitted to the National Office must include an analysis and a recommendation by the State Office.

If you have any questions, please contact the Business and Industry Division, Loan Processing Branch, at (202) 690-4103.

(Signed by Ben Anderson)

BEN ANDERSON
Administrator
Business and Cooperative Programs