



FactSheet

Extension

Ohio State University Extension Fact Sheet

Community Development

2120 Fyffe Road, Columbus, OH 43210-1010

Administering a Revolving Loan Fund

CDFS-1230-97

Small Business Series

Marianne M. Huey

Introduction

This fact sheet provides basic information on administering a Revolving Loan Fund (RLF) program utilizing public funds, and is targeted toward economic development practitioners. RLF's may be found throughout the State of Ohio, capitalized by a variety of public sources, each with its own unique structure and set of criteria. Program administration is a critical element of the Revolving Loan Fund Plan (See Fact Sheet CDFS-1229, "Establishing a Revolving Loan Fund"). The Plan addresses such areas as:

- Who will administer the program?
- Staff capacity and responsibilities
- Marketing strategies
- Loan selection and approval process
- Loan Servicing
- Capital management strategy
- Sources of funding to cover administrative costs
- Loan Review Committee

- Other requirements
- Effective administration is the key to program success. The loan administrator should network with other programs administrators and collect samples of application forms, legal documents, checklists, and other materials. Over time, these resources may be used to fine-tune the administrative process and RLF "paperwork."

The RLF Application

There are several ways to prepare a loan application package. Ultimately, the purpose of the application is to request specific information necessary to make an accurate assessment of the funding request.

Starting with a Pre-App

Since many businesses request information on sources of financing available for their company's needs, it may be prudent to offer a pre-application to potential borrowers. The pre-application is designed to make a preliminary determination on the merits of the project and the needs of the individual borrower. Typically, it is one or two pages in length, and asks for the following:

Information on the borrower:

- name
- address
- phone number
- Information on the business:
 - name
 - address
 - phone number
 - number of employees
 - type of business (SIC Code)
 - type of business organization
 - Tax ID number
 - date established
 - number of jobs to be created

For a New Business:

- Has a business plan been prepared? (if so, ask for a copy)
- Financing Information:
 - Amount of the loan request

- Total project cost
- Purpose of the loan request
- Use of proceeds
- Amount of equity available for the project
- Name of financial institution and contact person/phone number
- Financial Statements (3 years)

Certifications:

- This final section certifies that the information in the pre-application is true and correct and has been submitted, with consent of the applicant, to the funding source for review.
- Typically, there are several clauses contained in the Certification section, such as those which prohibit discrimination by the funding agency, authorize the collection of additional information about the applicant, or provide a liability disclaimer. Depending on the source of capitalization for the RLF, there may be specific Federal Regulations which need to be cited or referred to for compliance.
- A place for the applicant's signature(s) immediately follows the Certification section along with the printed name and date. It is important to clearly state where the application may be submitted and/or where questions may be directed on the form. Completed applications should be date stamped when received and a letter sent to the potential borrower indicating receipt of the application.

The Full Application

Once it has been determined (from the pre-application) that the applicant is an eligible borrower and that the proposed project fits the criteria of the RLF program, a full application is requested. While the pre-application contains basic information on the business and proposed project, the full application is much more detailed and requires attachments and supporting documentation. The basic components of a full application include:

- Information on the borrower, including a brief history of the company;
- A Business plan (required of a start-up) and/or marketing plan--information on the business which discusses the major products or services offered and identifies existing and potential customers and competitors (see Small Business Fact Sheet 1101-94, Organizing a Business Plan, for more information);
- Personal financial statements and tax returns--required of sole proprietorships, partnerships, and corporations. In the case of corporations, documentation is

requested from each of the principals owning 20% or more of the outstanding stock in the company. Personal tax returns should include three prior years;

- Historical financial statements including the profit and loss (income statements) and balance sheets for the three prior years. Interim statements, not more than 90 days old, are also advised. If the company is small, the administrator should obtain three prior year's tax returns on the company if no formal financial statements exist;
- Three years projected financial statements, including profit and loss, balance sheet, and cash flow analysis. The first two years should be monthly and the third year may be quarterly;
- Resumes of principals;
- Schedule of existing business loans;
- A description of the machinery and equipment (to be purchased) and/or working capital, if applicable;
- Documentation of the business entity--this demonstrates authorization to sign a loan agreement. For corporations, obtain a copy of the Articles of Incorporation, a Resolution of the Board of Director's, and a copy of the Corporate By-Laws. (NOTE: It is important to verify that the Corporation is in good standing. In Ohio, the Secretary of State's office may be contacted as part of the documentation process at (614) 466-3910.); and,
- A Letter of Commitment from a financial institution--documentation must be provided that details the amount of the loan, term, interest rate, collateral, conditions, and that the loan has been approved. For publicly-funded RLF programs, the letter from the financial institution must include a statement that without the assistance of the Revolving Loan Fund, the project would not proceed. Remember, the purpose of the RLF is to provide "gap" financing. If the borrower is able to finance the project entirely through private sources, public funds should not be involved.

Loan Evaluation

Upon receipt of a complete application and supporting documentation, the Loan Administrator (or an authorized designee, such as a Financial Consultant) conducts a credit analysis and determines preliminary underwriting standards for the project.

An important part of the evaluation process is to meet with the business and the participating lender. The purpose of the meeting is to review the application, clarify areas of uncertainty, and reaffirm the bank commitment toward the project.

The following areas need to be considered as part of the loan evaluation:

1) Credit

After review of the historical financial statements and/or reasonable projections, does the applicant demonstrate the ability to repay the loan?

2) Collateral

Is there sufficient collateral available to cover the bank financing and the RLF financing? If not, is additional collateral available which may be put toward the project?

3) Character

Has the applicant demonstrated a reasonable approach to business? Are personal and professional references available? Do you feel comfortable with the integrity of the borrower?

4) Management

Is the company successful? Does management demonstrate knowledge in a wide variety of areas necessary for company success? (production, marketing, sales, etc.)

5) Guarantees

Personal or corporate guarantees demonstrate commitment to the project. When evaluating guarantees, consider the following: the net worth of the guarantor; the liquidity of the guarantor; any contingent liabilities; and, whether or not the assets securing the guarantee can be moved. For many RLF's, personal guarantees are required.

Loan Structuring

Once the credit analysis is conducted, and it is determined that the borrower is able to repay the funds, the loan is structured, based on the following:

- Use of Funds

State what the RLF funds will be used to finance: acquisition of land, building, machinery and/or equipment; new construction; remodeling; inventory; working capital; etc.

- Maximum Loan Amount

State the maximum amount the RLF will lend on the project.

- Rate

Indicate the proposed interest rate for the RLF dollars loaned and whether the interest rate is fixed or variable for the term of the loan.

- Term

State the length of the loan in years. Typically, the term of the RLF loan is equal to the bank term. General guidelines are as follows:

Equipment --up to 10 years or based on the useful life of the asset

Real Estate--15 to 20 years

Working Capital--up to 3 years

- Collateral

Indicate the assets being pledged as security for the RLF financing.

Generally, RLF's take a subordinate position to the primary lender on the assets financed.

- Bank Participation

State the amount of bank financing in the project, the interest rate, terms of the financing, and the collateral being taken as security for the loan.

- Equity

Indicate what the borrower is investing in the project.

- Other Criteria

This section lists other program thresholds which must be met by the borrower as part of the loan agreement. It may include job creation goals and project completion deadlines, for example.

Loan Approval Process and Closing

The completed application and structured loan is then taken to the Loan Review Committee for its review and approval and/or disapproval. At this point, it is the responsibility of the Committee to verify that the rules and regulations governing the application process, contained in the RLF Plan, have been met, and that all documents are in order.

Most importantly, the Committee sets the terms and conditions of the loan. The proposed interest rate and term may be altered, additional collateral requested, or other such conditions placed on the borrower. The purpose is to safeguard the position

of the Grantor while at the same time, provide the needed "gap financing" to make the deal happen. A resolution recommending the project be funded is adopted by the Loan Review Committee, signed by the Chairperson, and recorded in minutes of the meeting. With most publicly-funded RLF's, the recommendation is then forwarded to the local governing body for final action.

The loan closing and disbursement of funds is primarily the responsibility of the Loan Administrator and the designated attorney for the program. Often, the local county prosecutor or city solicitor can be recruited to serve as the RLF attorney. Proper loan documentation is critical to the success of the program, because it improves the Loan Administrator's ability to recover funds in case of default. Each project will have its own particular set of applicable closing documents. The following items should be considered:

- Loan Agreement
- Promissory Note
- Security Agreement
- Mortgage (real estate)
- UCC's (Uniform Commercial Code Financing Statements) (equipment)
- Subordination Agreement
- Personal Guaranty
- Title Insurance
- Articles of Incorporation/Partnership Agreement
- Corporate Resolution
- Good Standing Agreement
- Key-man Life Insurance (when applicable)
- Opinion of Counsel

Loan Servicing

There are many tasks involved in loan servicing, including: collecting and tracking payments; receiving and evaluating annual financial statements; verifying proper insurance; handling late payments; renewal of UCC filings; and, structuring work-outs. Establishing well-organized files will facilitate the monitoring process for the Loan Administrator. The servicing file should contain the following:

- A cover sheet which explains the specifics of the loan--name of borrower, amount, rate, term, collateral, etc.
- Loan Amortization schedule
- Payment record--including payments received, date, amount allocated to interest and principal, accumulated past due interest, outstanding principal balance.

- Copies of insurance coverage
- Copies of annual financial statements
- A "notes" section to track all contacts with the business.
- When a payment is received by the Loan Administrator, the check should be immediately stamped "for deposit only" and a copy made for the borrower's file. Checks should be deposited within 24 hours of receipt.
- A "tickler system" should be established to keep track of items in the file which have due dates. Loan repayments, insurance renewals, and real estate taxes are important items to monitor. In addition, UCC's must be refiled every five years with the County Recorder's Office. And, there may be loan covenants placed on the borrower which must be completed within a certain time frame. These may include project completion and job creation deadlines.
- Keeping an accurate record of loan repayments will assist in the early detection of late payers and potential "red flag" issues. To facilitate the recording process, it is recommended that a standard payment date be established for all borrowers. If a check is not received by the due date, a late payment notice should be sent and penalties enforced as per the policies detailed in the RLF Plan.

Where to Go for Help

The Ohio Department of Development, Office of Housing and Community Partnerships, has a Revolving Loan Fund Coordinator who is responsible for overseeing RLF's capitalized with Community Development Block Grant funds within Ohio. Sample guidelines and forms are available, as well as a listing of the counties and cities which have Revolving Loan Fund programs.

The National Association of Development Organizations (NADO) conducts two training courses on revolving loan funds. One focuses on "Program Development," which explores the strategic decisions used in setting up a program. The other concentrates on the variety of tasks involved in "Program Management." For more information on these courses and others, contact:

Jonathan Corso
NADO
444 N. Capitol
Washington, DC 20001
Phone: (202) 624-7806
Fax: (202) 624-8813

Finally, a three-day training course entitled, "Revolving Loan Funds: Design, Documentation, and Administration" is offered through the National Development Council (NDC). This in-depth program covers such topics as: Revolving Loan Fund Design; Credit and Collateral Analysis; Closing and Documenting Loans; Servicing and Portfolio Management; and, Workout Strategies. For more information, contact the Training Division, National Development Council, 211 E. Fourth Street, Covington, KY 41011, (606) 291-0220, FAX (606) 291-3774.

All educational programs conducted by Ohio State University Extension are available to clientele on a nondiscriminatory basis without regard to race, color, creed, religion, sexual orientation, national origin, gender, age, disability or Vietnam-era veteran status.

Keith L. Smith, Associate Vice President for Ag. Adm. and Director, OSU Extension.

TDD No. 800-589-8292 (Ohio only) or 614-292-1868

| [OhioLine](#) | [Search](#) | [Fact Sheets](#) | [Bulletins](#) |