



Revolving Loan Funds: When the Deal Goes Bad



National Development Council

Partners in Community Development Since 1969



NDC's work focuses on HOMES, JOBS and COMMUNITY. Founded as a national nonprofit in 1969, NDC has worked for almost 50 years fulfilling its mission to increase the flow of capital for investment in low-income communities. NDC directs capital to support the development and preservation of affordable housing, the creation of jobs through training and small business lending and the advancement of livable communities through investment in social infrastructure.



HOMES JOBS COMMUNITY



IMPACT AT A GLANCE

\$632M
for Affordable
Housing

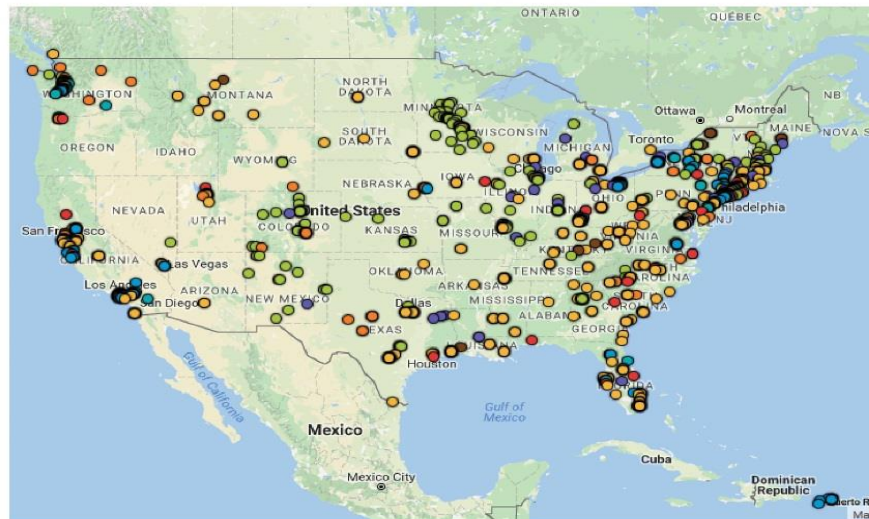
\$704M
in New Markets
Tax Credit
Allocation

\$2.6B
in Public-Private
Partnership
Development

\$212M
in Small
Business Loans

70K+
Practitioners
Trained

100+
TA Client
Communities



Grow America Fund

The Grow America Fund (GAF) was established in 1992 and is the nation's only U.S. Small Business Administration licensed small business lending company (SBLC) owned and operated by a nonprofit organization.

GAF operates in more than 50 communities across the nation, from Wilmington, DE to Los Angeles, CA to the Commonwealth of Puerto Rico to Seattle, WA.



\$220 Million

loaned

average loan:
\$379,310



580

loans to small
businesses



14,036+

jobs created and
retained

But... How many deals have gone bad?

Grow America Fund Default Rates:

- 2.6% based on the dollar amount written off
- 6.9% based on the number of loans written off

Loans in liquidation represent 2.2% of the total portfolio and are in an active work out or restructure phase.



\$6.1 Million

Written off



40

loans



\$5.2 Million

19 Loans

In Liquidation

City of Long Beach EDA RLF

The City of Long Beach EDA RLF was established in 2002 and is managed by the city's Economic and Property Development Department with assistance from the Finance Department and the City Attorney.

LB EDA RLF was started to help displaced workers after losing more than 50% of its employment base during the 1990's when Boeing and the LB Naval Station & Shipyard closed large manufacturing operations within the city.



\$5.1 Million

loaned

average loan:
\$90,368



57

loans to small
businesses



328+

jobs created and
retained

But... How many deals have gone bad?

Long Beach EDA RLF Default Rates:

- 7.1% based on the dollar amount written off
- 12.3% based on the number of loans written off

Restructured loans represent 2.8% of the total portfolio and are in active repayment mode again.



\$366,737

Written off



7

loans



\$145,630

5 Loans

Restructured

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What are the standard loan collection procedures?

- Loans are serviced by Finance Department and a loan servicing agency (Weststar)
- Coupon books for monthly payments are provided
- ACH electronic payments are highly encouraged
- Late charges for 10 days or more past due
- Late fees are 5% or \$50, whichever is greater
- NSF fee is \$25 for returned checks

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What are the standard delinquency procedures?

- Late payment letter is automatically sent to the borrower after 10, 30, and 60 days of delinquency
- Staff is to make personal contact with the borrower within 60 days
- Perform site visit to inventory collateral and discuss resolution to delinquency
- Negotiate restructure agreement and/or loan modification with input from City Attorney, if necessary
- If no resolution after 90 days delinquency, loan will be put into default and referred to City Attorney

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What are typical loan restructure/modification options?

- Change/extend the term of loan to allow for more repayment time and/or lower monthly payment amount
- Waive late fees to lessen repayment burden
- Lower interest rate (not as common)
- Add/remove personal guarantors due to change in ownership (tread cautiously)
- Negotiate settlement amount for lump sum payment

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What are default procedures?

- **Send Demand Letter to borrower**
- **Send legal notifications to guarantors and other lenders**
- **Seize and liquidate business assets pledged under a UCC filing**
- **File for a judgement against borrower in court**
- **Default judgement granted if borrower does not appear in court**
- **Abstract of judgement is recorded with County Clerk (must be re-recorded every 10 years)**

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What are the realities of collection?

- Due to limited options, it is extremely difficult to recover ANY loan funds in a default scenario
- Costs associated with seizing business assets pledged under a UCC filing (\$5-10K) are typically greater than the value that could be liquidated from the assets (aka not worth it)
- Legal action usually doesn't garner much action or payment on the part of the borrower
- It's hard to execute on the judgement after it is filed because borrowers do not have any assets
- Most borrowers do not declare bankruptcy so there is no legal procedure for satisfying debtors

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What are the benefits of filing a legal judgement against the borrower?

- **If they own real estate, proceeds from the sale of real estate will be held in escrow and the judgement amount would get paid out of proceeds before they are released to the borrower**
- **Public Filings are listed on a borrower's credit report, adversely affecting their personal credit score and hindering future borrowing capacity**

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Examples of Collections in Default

- **20% of outstanding loan balance collected during bankruptcy proceedings**
- **Borrower calls up after 5-6 years to negotiate settlement and release of legal judgement in order to proceed with new loan/property acquisition/business venture/etc.**
- **Waive all late fees and accept 50% settlement on loan balance in a lump sum payment**

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What are the lessons learned?

- Servicing an RLF is typically too labor intensive for city staff or smaller organizations
- Outsourcing servicing is relatively affordable (ex. \$400/mo. for LB EDA RLF)
- Make the effort to follow legal bureaucracy of the courts because you never know when or how you might be able to recover some loan funds
- Example: 10 hours/yr. spent on defaults by LB EDA RLF City Attorney

Contact Information

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We are happy to answer any questions you have!

Andria Martinez

amartinez@ndconline.org

(805) 698-8005

Diana Sasser

dsasser@ndconline.org

(209) 483-9863

www.ndconline.org