Business Engagement and Compliance Office
DBE Supportive Services

2013

Financial Services Handbook for Small and Disadvantaged Businesses

Compliance is our Driver, Opportunity is our Destination

ADOT

> “Small and disadvantaged businesses learn about the alternative financial services available to them.”

Financial Services Handbook for Small and Disadvantaged Businesses

Department of Transportation Business Engagement and Compliance Office

INTRODUCTION

Small and disadvantaged businesses frequently cite lack of financing, insurance and bonding as barriers to their growth and success. The purposes of this *Financial Services Handbook* are to help small and disadvantaged businesses learn about the alternative financial services available to them, and how to access them.

The first part of this booklet describes financing alternatives. The second part addresses insurance services and the third part describes different kinds of bonds. While the author has attempted to use plain language whenever possible, a glossary at the end defines some of the technical terms used.

ADOT is providing different resources to assist Disadvantaged Business Enterprises and small businesses in doing work within their industries. ADOT is not endorsing any organization or company. All resources in this Handbook are compiled from a network of readily available sources. Businesses should analyze their own financial status before choosing which direction to proceed when looking for capital, insurance and bonding.

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DBE Supportive Services

The DBE Supportive Services program is designed to assist qualified minority- and woman-owned businesses to become certified as Disadvantaged Business Enterprise (DBE) firms. Once certified, the program strives to assist DBE firms to get work on federal-aid contracts and to become self-sufficient in their respective industries. A variety of training programs and technical assistance is provided by the Supportive Services program staff to assist DBEs in meeting these goals.

Companies registered as Small Business Concerns (SBC) can also participate in conferences and trainings offered to DBEs.

You can also contact us at 602-712-7761 or email DBESupportiveServices@azdot.gov if you would like to be added to our email list to be notified of upcoming events or if you have any questions or need assistance.

FINANCING

Reasons for Financing

Financing is a tool for businesses to grow; it is not a good tool for businesses to use just to survive. Before seeking financing, business owners should assess why financing is needed, how it will help the business grow, and what kind of financing will best suit its growth opportunity.

Many businesses need financing from time-to-time. Reasons for a business to borrow money include:

- *Working capital* is money needed to buy inventory and pay routine expenses before sales revenues are collected; it is the difference between "cost of goods or services sold" and revenue collected later as a result of those expenses. The ideal way to finance working capital is with the owner's initial investment, rather than a loan. But a growing company will need much more working capital, and may seek a conventional bank loan or an SBA-guaranteed "CAPLines" bank loan, which is designed for these purposes.

- *Cash flow* is the ins and outs of money through the business. Businesses with regular, consistent expenses (payroll, rent, utilities, supplies, *etc.*) and "lumpy" revenues, because of seasonal variations or project schedules, often have cash flow deficits. To meet expenses when due, even though revenues have not yet come in, companies may borrow money on a short-term basis, and pay off the short-term loan when the revenue comes in. Companies that are growing rapidly will need more cash flow financing than companies that are stable. A line-of-credit (LOC) is a good vehicle to meet variable cash flows.

- *Business expansion:* Expansion can sometimes take advantage of economies of scale, increasing revenue without increasing administrative overhead. Financing can provide leverage to access new markets, create new products and services or establish new locations. Expansion may require a conventional bank loan or SBA-guaranteed "7(a)" bank loan.

- *Real estate:* Some businesses require real estate to operate, such as an equipment yard, office, warehouse or factory space. If owning real estate is better than leasing it, an SBA-guaranteed "CDC 504" loan may be appropriate.

- *Capital outlay:* Some businesses can project greater profits or revenues, or lower costs, if they can acquire capital equipment (things that will last 3-5 years or more). It may be a new backhoe, a dump truck, or a digital copier. For capital outlays, several options include: conventional bank loan; for smaller amounts ($5 million or less), an SBA-guaranteed "7(a)" bank loan; for larger amounts, an SBA-guaranteed "504" loan; an equipment lease.

- *Collateral:* Virtually all loans require a pledge of assets worth at least as much as the loan as collateral. Real estate and equipment are their own collateral. Working capital and cash flow loans are often based on all assets of the business including accounts receivable.

Types of Loan Financing

Business borrowers should choose the type of loan financing that best suits their purpose:

- *Line of Credit:* An LOC is a type of business bank loan used primarily to finance irregular cash flows. The business must pay interest on the principal balance every month, and banks expect the business to pay down the entire LOC at least once a year. Interest rates will float about 8-10 percentage points above a standard such as the prime rate, or a greater spread above the LIBOR. It generally requires a good credit rating, operating history, personal guarantee and collateral.

- *Government-guaranteed loans.* The U.S. Small Business Administration, Department of Transportation, Department of Agriculture and Bureau of Indian Affairs all have programs that guarantee greater parts of small business bank loans. For this guarantee, the borrower pays a fee based on the amount of the guarantee. The guarantee reduces risk to the bank making the loan and may reduce interest costs.

› *Conventional loan:* Banks also make conventional loans to businesses that are not guaranteed by SBA or other agency. Conventional loans may not follow all the rules required by SBA. Banks may charge fees and points on these loans, but not the guarantee fee. Conventional loans may charge higher interest rates than allowed on government-guaranteed loans.

Borrowers should evaluate carefully which type of loan is better for them: a government-guaranteed loan with a guarantee fee and low interest rate, or a conventional loan with fees, points and interest rate.

LENDERS

Most small businesses will finance their capital needs with loans. Lenders take different forms:

Banks

Banks are a source for most small business financing, including both conventional loans and government-guaranteed loans, such as SBA-guaranteed loans.

Banks make their money by earning interest on loans. They do not generally take risks; investors may take risks, but not banks. Banks set up a three-tiered structure to make sure they get repaid the principal plus the interest on the loan:

› *Sound business:* A bank first looks to the borrowing business to service (pay principal and interest on) a loan. It will analyze the business' accounting statements and tax returns to determine if the business will be able to make payments. It will look at how the intended uses of the loan proceeds will benefit the business. The bank may ask for a business plan describing how the loan proceeds will improve the business and enable it to make principal and interest payments.

› *Collateral:* The bank will require the business owners to pledge assets as collateral to secure the loan. Equipment or real estate will usually be their own collateral. For other purposes, collateral may include fully paid-for vehicles or equipment, real estate owned free and clear, or securities such as a certificate of deposit the business or its owners may have. Real estate improvements, machinery, equipment and vehicles must have insurance. Lenders will file a lien against real estate and registered vehicles used for collateral, preventing sale until the loan is paid off.

Small businesses located within the City of Phoenix may be able to use the Expansion Assistance and Development ("Expand") program. The City will post up to 25% of the collateral needed, to a maximum $150,000, for up to four years. Businesses must create one permanent job for each $35,000 of collateral provided, and invest at least 10% equity in the project. Eligibility is similar to SBA's Basic 7(a) program. Details are at phoenix.gov/econdev/growbus/expandassist.

› *Personal guarantee:* The bank will require owners of 20% or more of the business to personally guarantee that loan payments will be made. If the business fails to make payments, and the collateral cannot be seized and sold or is not worth enough to cover the loan balance, the bank will look to the owners to make payments from their personal resources.

If a loan is government-guaranteed, the bank has a fourth tier of protection. The U.S. Small Business Administration (SBA), U.S. Department of Transportation (DOT), U.S. Department of Agriculture (USDA), and the Bureau of Indian Affairs (BIA) all have programs to guarantee loans to small businesses.

Banks that offer SBA loans have three levels of relationship with SBA:

› *Preferred Lenders Program (PLP)* participating lenders can make final credit and other decisions regarding loans without first consulting the SBA, though the SBA retains responsibility to check loan eligibility.

- *Certified Lenders Program (CLP)* participating lenders receive expedited (three working days) decisions from SBA regarding credit and eligibility. SBA counts on the CLP lender to conduct a credit analysis, so SBA conducts a less-time-consuming credit review.

- *General Partners (GP)* submit applications to SBA for review and approval. Loans submitted to General Partner lenders may take longer to process and to reach a final decision than loans submitted to PLP or CLP lenders; still, most loans are processed in two weeks or less.

Regardless of the lender's relationship level, the SBA reviews all loans for eligibility, and many loans for creditworthiness. The relationship level is not necessarily a reflection of the lender's quality; some excellent lenders choose not to participate in the PLP or CLP because it opens their books to government auditors.

Two kinds of banks serve most markets: The "big four" national banks have lots of branches and hundreds of billions of dollars in assets. They include Bank of America (www.bankofamerica.com) Chase Bank (www.chase.com), Citibank (www.citibank.com; not in Arizona) and Wells Fargo (www.wellsfargo.com). In the other group are community banks, which generally have one or several branches. They may be independent, or owned by a holding company that owns several banks, many with different names.

The "big four" banks have nearly unlimited resources, extensive experience, and make lots of loans to small businesses. Community banks have a clear understanding of the local market, compete actively for business loans and emphasize customer service.

Community Advantage Lenders

A Community Advantage (CA) lender is designated by SBA to serve small businesses in underserved markets. They are primarily not-for-profit organizations focused on economic development, including Certified Development Companies (CDCs), Microloan Intermediaries and Community Development Financial Institutions (CDFIs).

CA lenders have some different terms than other SBA lenders:

- CA lenders may make SBA-guaranteed 7(a) loans up to a maximum $250,000.

- They are allowed to charge higher interest rates than banks, up to prime plus 6%.

- They may not issue revolving lines of credit.

- Application and closing processes may be different.

Factors (Accounts Receivable Funding)

A factor helps businesses meet short-term cash flow needs by purchasing their accounts receivable at a discount.

Advantages of accounts receivable funding are: simple application, quick funding, usually no credit check, and the collateral is the invoice. The disadvantage is that factors are often more expensive than bank loans.

For example: A subcontractor hauls dirt for a highway project and bills the prime contractor. The prime contractor waits until the end of the month to bill the project owner, the Arizona Department of Transportation. ADOT may take two weeks or more to pay the prime contractor. The prime contractor then pays its subcontractor within seven days (www.azleg.gov/ars/32/01129-02.htm). Any disputes can extend the times.

A subcontractor who does not want to wait may sell the account receivable to a factor, for example, at 98 cents on the dollar – a discount of 2% – for a receivable expected to be paid in three weeks. The subcontractor gets almost all the money quickly, usually in just a day or two. The factor will ask the prime contractor to send the payment directly to the factor.

The discount the factor charges the subcontractor depends on how big the advance is, how long the factor has to wait for payment and the likelihood that the factor will receive payment on time.

From the subcontractor's perspective, the factor's discount is like interest on a short-term loan. An interest rate is the price of the money over time. To calculate the effective annual interest rate based on a factor's discount, divide the number of days in a year (365) by the number of days until payment is expected (21 days in the example): 365 ÷ 21 = 17.4, which is the number of 21-day periods in a year. Then multiply the result (17.4 in the example) times the discount (2% in the example): 17.4 x 0.02 = 0.35 = 35% effective annual interest rate.

Leasing Companies

For expensive capital equipment outlays, a leasing company may purchase the equipment and lease it to the business. The business pays a fixed amount monthly, and may have an option to purchase the equipment at a lower, "depreciated" value at the end of the lease. Like auto leases, lease payments may be lower than principal and interest payments on loans, *but they do not convey ownership*. Like loans, leases will typically require a credit check and a personal guarantee. The equipment being leased is the collateral.

Joint Checks

Small businesses may have difficulty fulfilling a contract because they do not have money to buy materials, and poor credit may prevent them from borrowing working capital. A joint check agreement may solve this problem, and are common practice in construction.

A joint check agreement has at least three parties, typically a prime contractor, a subcontractor and a materials supplier. The supplier advances materials to the subcontractor with the agreement that the prime contractor's payment check will be made out jointly to both the subcontractor and the supplier. Both parties must endorse the check for either one to be paid, so the supplier can ensure payment at the same time the subcontractor is paid.

A joint check agreement must be in writing and cover a specific time period. If the agreement is for an ADOT-funded project: all parties must be independent of each other; the Business Engagement and Compliance Office must approve it: payment reports must include copies of cancelled joint checks; certificates of payment must indicate whether joint checks were used; all three parties must report any changes in the agreement. Regulations are at www.azdot.gov/docs/default-source/beco-library/adot_fhwa_dbe_plan_052512.pdf, page 19.

The advantages of joint checks are: subcontractors with poor credit can fulfill contracts; subcontractors may develop business relationships with materials suppliers leading to favorable payment terms in the future; suppliers are assured of payment; prime contractors are assured that a supplier will not file a lien on the project due to non-payment.

Disadvantages of joint checks include: endorsing a joint check may create a legal presumption that the payees have been paid in full, even though they may not have received all payments due; the payees may argue over how the payment is to be allocated between them; some parties have been known to forge the other payee's endorsement, or a bank may mistakenly deposit a joint check without both endorsements; the agreement may make the prime contractor a guarantor of payment to the supplier; if one party files bankruptcy before endorsing a joint check, ownership of the interest in the check is in doubt.

A carefully-written joint check agreement can overcome these disadvantages. Attorneys should prepare and review these agreements to ensure they protect all parties' rights and meet state laws and regulations.

SBA-GUARANTEED LOAN TERMS

SBA-guaranteed loans are bank loans, not government loans. Apply with almost any bank. SBA-guaranteed loans fall into two major types: 7(a) loans for working capital, operations, expansion or exporting, and CDC 504 loans for real estate and long-term capital equipment.

A list of the major SBA lenders in Arizona is on page 11. A list of all active Arizona SBA lenders is at: www.sba.gov/sites/default/files/Lender List AZ V16.6 website.pdf.

SBA-Guaranteed Basic 7(a) Loan Program Terms

Eligibility: In general, applicants must: be a U.S. for-profit small business (for contractors, under $14 million annual revenue) with invested equity; use alternative resources before seeking a loan; demonstrate a sound business need for loan proceeds; not be delinquent on taxes or other government debt; and not be in one of these industries: financial services, multi-level marketing, gambling, lobbying, rare coins and stamps, real estate investment, religious education, strip club or speculative industries like oil exploration.

Allowed uses of loan proceeds include: long-term working capital for operations; short-term working capital, such as seasonal financing, contract performance, construction financing or exporting; revolving funds for inventory and receivables; equipment, machinery, furniture, fixtures, supplies or materials; real estate land and buildings; construction or renovation; create a new business; buy, operate or expand an existing business; refinance business debt in some cases.

Disallowed uses include: refinance a debt that would transfer a loss to the SBA; change in ownership that does not benefit the business; reimburse an owner for money invested in or borrowed by the business; pay delinquent taxes or money held in trust or escrow; or unsound business purposes.

Collateral: SBA-guaranteed Basic 7(a) loans generally must be fully secured with collateral. Owners of 20% or more must provide a personal guarantee; other owners may be asked for a personal guarantee.

Guarantee percentage: SBA guarantees 85% of the loan amount up to $150,000, and 75% for larger loans. SBA Express loans have a maximum guarantee of 50% (see below).

Guarantee fee: SBA charges borrowers a fee based on the amount of the guarantee and the term of the loan. Banks may not charge other fees or points beyond the guarantee fee on SBA-guaranteed loans (see table).

Interest rates on SBA-guaranteed Basic 7(a) loans have a base rate, and banks then add a "spread" (see table). The base rate is either the (a) prime rate, (b) LIBOR plus three percentage points or (c) SBA Peg Rate (see Glossary).

Loan amount for Basic 7(a) loans is up to $5 million. The average loan is between $300,000 and $400,000.

Maturity: SBA-guaranteed Basic 7(a) loans usually mature in seven years or less. Equipment loans are tied to the useful life of the equipment, up to 10 years. Real estate loans mature in up to 25 years. Short-term loans and revolving lines of credit may also be available.

Payment terms: Basic 7(a) loans require monthly payments of both principal and interest. Loans for business startups or expansions may include interest-only payments early on. Revolving line of credit payments can be interest-only. Prepayment penalties are charged only for loans maturing in 15 years or more and paid off during the first three years.

Other SBA-Guaranteed 7(a) Loan Programs Terms

In addition to Basic 7(a) loans, SBA has several special types of 7(a) loans. These special types have the same eligibility, allowed uses, collateral, guarantee fee, interest rates, loan amounts, maturities, payment terms and other requirements as Basic 7(a) loans, except as noted below:

CAPLines: Up to $5 million to help small businesses meet short-term and cyclical working capital needs. CAPLines includes four types of loans:

a. *Contract Loan Program:* Used for direct costs of performing construction, service and supply contracts, subcontracts, or purchase orders; maturity is based on the length of the contract; may revolve up to 10 years; contract payments are sent directly to the lender.
b. *Builders Line:* Use for direct cost associated with commercial and residential new construction or remodeling when buyer is not known; can include land up to 20% of loan proceeds; matures in three years, or extended to five years.
c. *Seasonal Line of Credit:* Seasonal working capital for inventory or accounts receivable; must pay off for at least 30 days after "season;" may revolve up to five years.
d. *Working Capital Line of Credit:* A revolving line of credit for short-term working capital, up to $5 million.

Small/Rural Lender Advantage (S/RLA) is a type of SBA-guaranteed 7(a) loan up to $350,000 with a streamlined, two-page application process. Some additional information will be required for loans above $50,000. Banks in rural areas fax loan applications to SBA, which expedites processing in three-to-five days.

SBA 7(a) Loans Guarantee Fee

	Maturity	
Guarantee Amount	**One Year**	**Less Than One Year**
$150,000 or less	2.00%	0.25%
$150,000-$700,000	3.00%	
$700,000 or more	3.50%	
Amount that exceeds $1 million	Additional 0.25%	

Base rate: Either (a) prime rate; (b) LIBOR plus three percent; or (c) SBA Peg Rate (see Glossary).

SBA 7(a) Loans Maximum Interest Rates

	Maturity	
Loan Amount	**Less than seven years**	**Seven years or longer**
$25,000 or less	Base rate plus 4.25%	Base rate plus 4.75%
$25,000-$50,000	Base rate plus 3.25%	Base rate plus 3.75%
$50,000 or more	Base rate plus 2.25%	Base rate plus 2.75%

SBAExpress loans up to $350,000 are reviewed by SBA within 36 hours. SBAExpress loans have a 50% guarantee, and mature in up to seven years plus possible extensions agreed at the time of the loan. Balloon payments are allowed. For loans of $50,000 or less the interest rate may not exceed 6.5% over the base rate, or for larger loans, not more than 4.5% over the base rate. Lenders are not required to take collateral for loans under $25,000, and may follow their own collateral policies for larger loans. Use the lender's own application forms, plus a Borrower Information Form, SBA Form 1919 (www.sba.gov/content/sba-express-export-express-small-loan-advantage-plp-caplines-and-pilot-loan-programs-partrio).

Patriot Express loans up to $500,000 are for military community members, including: veterans and service-disabled veterans; active-duty service members, reservists and National Guard members; current spouses of any of the above; or veterans' widows if the veteran died during service or of a service-connected disability. Collateral requirements are the same as for SBAExpress loans, except loans from $350,000 to $500,000 must be fully collateralized.

Microloans up to $50,000 (average about $13,000) are for small businesses and some not-for-profit child care centers to start-up and expand. They are available only through designated not-for-profit community-based organizations, (www.sba.gov/sites/default/files/Intermediary-List.pdf). Microloans can be used for working capital, inventory, supplies, furniture, fixtures, machinery or equipment, and they mature in up to six years. Interest rates fluctuate, and are generally between eight and 13 percent. Microlenders generally require collateral and a personal guarantee.

Export Working Capital Program (EWCP) loans are for businesses needing working capital to support international export sales. They are typically a revolving line of credit maturing in 12 months or less. They carry a 90% SBA guarantee, but the guarantee is limited to $4.5 million. A fixed or variable interest rate is negotiated between lender and borrower. Collateral can be the inventory and accounts receivable generated by the export sales being financed. Submit EIB-SBA Form 84-1 *Joint Application for Export Working Capital Guarantee* (www.sba.gov/content/joint-application-export-working-capital-guarantee) and attachments listed on page 12 of that form.

SBA-Guaranteed CDC 504 Loan Program Terms

A CDC 504 loan consists of a 50% loan from a bank, plus 40% loan from a Community Development Company (CDC; see list below) fully guaranteed by SBA, plus 10% down payment from the business owner.

Eligibility: A for-profit business doing business in the U.S. or its possessions, with tangible net worth less than $15 million and average net income less than $5 million for the preceding two years. Businesses must have relevant management expertise, feasible business plan, ability to repay the loan on time from projected operating cash flows and not have funds available from other sources. Ineligible companies are the same as for Basic 7(a) loans.

Allowed uses: CDC 504 loans are for real estate buildings, land or improvements, or long-term capital equipment.

Collateral: The real estate or equipment is the collateral. A personal guarantee from each owner is also required.

Guarantee fee: Approximately 3.0% of the amount of the guarantee.

Interest rate is pegged to an increment above the current market rate for 5-year and 10-year U.S. Treasury bond issues.

Loan amounts depend on how funds will be used, and which of the following program goals they support:

› *Job creation:* Maximum loan is $5.0 million. Business must create one job for every $65,000 guaranteed; small manufacturers must create one job for every $100,000 guaranteed.

› *Public policy*: Maximum loan is either (a) $5.5 million for small manufacturing, energy reduction or alternative fuels, or (b) $5.0 million for other public policy goals, including: business district revitalization; export expansion; minority business development; rural development; increased productivity and competitiveness; meet mandated federal standards or policies; respond to federal budget cuts; expand small business owned and controlled by women or veterans, especially service-disabled veterans.

- *Small manufacturing:* Maximum loan is $4.0 million for companies classified in NAICS codes 31, 32 or 33, with all production facilities located in the U.S. Must also either (a) create at least one job per $100,000 guaranteed by the SBA, or (b) improve the local economy or achieve one or more public policy goals described above.

Maturity: Either 10 or 20 years.

Payment terms: Repay principal and interest monthly.

SBA Disaster Loan Program Terms

Businesses in a declared disaster area experiencing uninsured damage may apply online directly to the SBA (disasterloan.sba.gov/ela/) for a low-interest loan up to $2.0 million for recovery. Business loans are available for both Business Physical Disaster losses (www.sba.gov/content/business-physical-disaster-loans) and for Economic Injury Disaster losses (www.sba.gov/content/economic-injury-disaster-loans). These loans are not bank loans and carry no fees. They must be collateralized if over $14,000 for physical disaster, or over $5,000 for economic injury disaster. Maturity is up to 30 years if credit is not available from other sources, or three years otherwise. Contact SBA for more details at 1-800-659-2955, disastercustomerservice@sba.gov or www.sba.gov/category/navigation-structure/loans-grants/small-business-loans/disaster-loans.

LOCATIONS OF ARIZONA CDCS

Business Development Finance Corporation
3300 N. Central Ave., Ste. 600
Phoenix, AZ 85012
Phone: 602-381-6292
Gary Molenda

Business Development Finance Corporation
335 N. Wilmot Road, Ste. 420
Tucson, AZ 85711
Phone: 520-623-3377

Southwestern Business Finance Corporation
3200 N. Central Ave. Ste. 1550
Phoenix, AZ 85012
Phone: 602-495-6495
Bob McGee

CDC Small Business Finance
2910 E. Camelback Rd., Ste. 185
Phoenix AZ85016
Phone: 800-817-3795
Christopher Bane

OTHER GOVERNMENT GUARANTEED LOAN PROGRAM TERMS

Three other agencies also have government-guaranteed loan programs:

U.S. DOT Short Term Lending Program Terms

Certified disadvantaged business enterprises, SBA-certified Section 8(a) small and minority- or woman-owned businesses, HUBZONE and businesses owned by service-disabled veterans are eligible for a line of credit up to $750,000 through the U.S. Department of Transportation (DOT), Short Term Lending Program (www.dot.gov/osdbu/financial-assistance/short-term-lending-program). The loan matures annually and may be extended up to five years. Collateral can include accounts receivable; personal guarantees and insurance will likely be required. Funds are borrowed against each invoice and payment occurs as the prime contractor or project owner pays the invoice. Lenders may charge reasonable fees, which cannot be added to the loan amount. Application documentation is similar to SBA-guaranteed loan application checklist.

Apply through Arizona's sole Participating Lender:

Préstamos CDFI
1024 E. Buckeye Rd, Suite 270
Phoenix, AZ 85034
Phone: 602-258-9911
www.prestamosloanfund.org/
Teresa Miranda, teresa.miranda@cplc.org

USDA Business & Industrial Guaranteed Loan Program Terms

Businesses in rural areas may apply for a Business & Industry bank loan (www.rurdev.usda.gov/BCP_gar.html) guaranteed by the U.S. Department of Agriculture (USDA) to improve, develop or finance business, industry and employment, and to improve the economic and environmental climate in rural communities. "Rural" areas include cities or towns of 50,000 or smaller population that are not next to a metropolitan area. Projects must have "tangible balance sheet equity" of 10% for existing businesses, 20% for start-ups and 25-40% for energy projects. Maximum loan amount is $10 million, or up to $25 million in rare cases. Maximum loan-to-value ratios are 80% for real estate, 70% for machinery and equipment and 60% for accounts receivable or inventory. Negotiated interest is not capped, but must be approved by USDA. Real estate loans mature in 30 years. Machinery and equipment loans mature based on the expected life of the equipment but not longer than 15 years. Working capital loans mature in seven years.

All loans are fully collateralized by the real estate, machinery, equipment or accounts receivable they finance, and by principal owners' personal guarantees. Loans of $5.0 million or less are 80% guaranteed; loans between $5.0 and $10.0 million are 70% guaranteed; loans above $10.0 million are 60% guaranteed. A 2% guarantee fee applies, plus an annual guarantee renewal fee, currently 0.25%. Application documents are the lender's own forms, and must include a business plan and project environmental information.

TOP SBA LENDERS IN ARIZONA

Alliance Bank of Arizona
1 E. Washington St., Ste. 1400
Phoenix, AZ 85004
Phone: 480-609-2914
Karen Goettl

Arizona Bank and Trust
4222 E. Camelback Rd., Ste. J100
Phoenix, AZ 85018
Phone: 602-840-3400
Sean Scibienski

Bank of America
201 E. Washington St.
Phoenix, AZ 85004
Phone: 800-432-1000

Bank of Tucson
4400 E. Broadway
Tucson, AZ 85711
Phone: 520-321-4500

BBVA Compass Bank
2850 E. Camelback Rd.
Phoenix, AZ 85016
Phone: 602-522-7536
Jim Hunter

BNC National Bank
20175 N. 67th Ave.
Phoenix, AZ 85308
Phone: 602-508-3760
Tim Collins

Business Development Finance Corp.*
3300 N. Central Ave., Ste. 600
Phoenix, AZ 85012
Phone: 602-381-6292
Gary Molenda

Capital Source Bank
28248 N. Tatum Blvd., Ste. B-1-458
Cave Creek, AZ 85331
Phone: 480-502-7950
Brad Berg

CDC Small Business Finance*
2910 E. Camelback Rd., Ste. 185
Phoenix, AZ 85016
Phone: 800-817-3795
Christopher Bane

Celtic Bank
268 S. State St., Ste. 300
Salt Lake City, UT 84111
Phone: 480-830-8444
Brenda Bevilacqua

Great Western Bank
1600 E. Florence Blvd.
Casa Grande, AZ 85222
Phone: 520-836-4666

Horizon Community Bank
225 N. Lake Havasu Ave.
Lake Havasu City, AZ 86403
Phone: 928-854-3000
Jeff Mizukami

JPMorgan Chase & Co.
201 N. Central Ave.
Phoenix, AZ 85004
Phone: 866-785-2821
Sheryl Cameron

Metro Phoenix Bank
4686 E. Van Buren St., Ste. 150
Phoenix, AZ 85008
Phone: 602-346-1800

MidFirst Bank
3030 E. Camelback Rd.
Phoenix, AZ 85016
Phone: 602-801-5344
Tom Altieri

Mountain America Credit Union
P.O. Box 9001
West Jordan, UT 84084
Phone: 602-538-9671
Bill Luckinbill

National Bank of Arizona
600 N. 24th St.
Phoenix, AZ 85016
Phone: 602-212-6459
Ward Hickey

Pinnacle Bank
14287 N. 87th St., Ste. 123
Phoenix, AZ 85260
Phone: 480-421-8919
Tim Romano

RepublicBankAZ
909 E. Missouri Ave.
Phoenix, AZ 85014
Phone: 602-277-2500
Stuart Olson

Seacoast Commerce Bank
2375 E. Camelback Rd., Ste. 600
Phoenix, AZ 85016
Phone: 602-387-5117
Shawn Greenway

Southwestern Business Financing Corp.*
3200 N. Central Ave., Ste. 1550
Phoenix, AZ 85012
Phone: 602-495-6495
Bob McGee

Stearns Bank
9225 E. Shea Blvd.
Scottsdale, AZ 85260
Phone: 480-314-4200
John Mistler

US Bank, NA
101 N. 1st Ave., Ste. 1600
Phoenix, AZ 85003
Phone: 602-241-9806
Doug Haman

Wells Fargo
100 W. Washington St.
Phoenix, AZ 85003
Phone: 602-378-5279
Jim Valley

* CDC 504 lender.

Other USDA-guaranteed loans are available for projects in rural areas related to energy production or not-for-profit small business financing organizations (www.rurdev.usda.gov/RD_Loans.html).

BIA Loan Guarantee Program Terms

For-profit businesses with 51% or more ownership by recognized Native Americans may apply for a bank loan up to $5.5 million, guaranteed up to 90% by the Bureau of Indian Affairs (BIA) under the Indian Affairs Loan Guarantee Program (www.bia.gov/cs/groups/xieed/documents/document/idc-034339.pdf). Loans may be used to finance commercial, industrial, agricultural or business activities that benefit Indian Reservation economies. Borrower must invest at least 20% of projects in cash or other free assets. Interest rate adjusts quarterly; maximum rate is 1.5% above the prime rate for a 90% guaranteed loan, or 2.75% above the prime rate for an 80% guaranteed loan. A further interest subsidy may be available for the first three years. Guarantee fee is 2.0% of the guarantee amount. Maturity depends on the use of proceeds and borrower's ability to repay the loan, not longer than 30 years.

For more information, contact:

Bureau of Indian Affairs
Southwest Credit Office Service Center
Phone: 505-563-5471
Shannon Loeve, Shannon.loeve@bia.gov
www.bia.gov/WhoWeAre/AS-IA/IEED/DCI/

SBA-GUARANTEED BASIC 7(A) AND CDC 504 LOAN APPLICATION CHECKLIST

Applying for an SBA-guaranteed loan requires a significant amount of paperwork. Put them in a folder or binder for the bank, and keep a copy!

- ❑ *SBA Application for Business Loan,* SBA Form 4 (www.sba.gov/content/application-business-loan). If your business is a corporation, stamp the corporate seal on the application form.
- ❑ *Statement of Personal History,* SBA Form 912 (www.sba.gov/content/statement-personal-history).
- ❑ *Personal Financial Statement,* SBA Form 413 (www.sba.gov/content/personal-financial-statement).
- ❑ *Business profit & loss statement* ("P&L;" also called "income statement"), year-to-date, no older than 90 days.
- ❑ *Business P&L* for last three complete fiscal years.
- ❑ *Projected business P&L* (also called *"pro-forma"* P&L) for one year after the loan. Show how the loan principal and interest will be paid from operating cash flows.
- ❑ *Written explanation* of how you expect to achieve the projection and service the loan in the projected business P&L.
- ❑ *Ownerships and affiliations:* List names and addresses of any subsidiaries, affiliates, concerns in which the business owners hold a controlling interest, and other concerns that may be affiliated by stock ownership, franchise, proposed merger or otherwise.
- ❑ *Business certificate or license,* if you have one; some Arizona cities require a business license; architects, contractors, engineers, geologists, surveyors, medical and judicial professionals and some others must have a state license.
- ❑ *Loan application history:* List any loans you have applied for in the past.
- ❑ *Federal income tax returns: Both* personal *and* business federal income tax returns for previous three years, for each principal owner.
- ❑ *Résumés* for each principal owner.
- ❑ *Business overview and history:* Write a brief history of the business and its challenges. Explain why the SBA-guaranteed loan is needed and how it will help the business.
- ❑ *Business lease,* or note from landlord with terms of the proposed lease.

If purchasing an existing business, also provide:

- ❑ *Current balance sheet and P&L* of business to be purchased.
- ❑ *Previous two years of federal income tax returns* for the business.
- ❑ *Proposed Bill of Sale,* including Terms of Sale.
- ❑ *Asking price* of business.
- ❑ *List* of inventory, machinery, equipment, furniture and fixtures, each with current values.

If this checklist on seems overwhelming, contact one of the following agencies for help. They will connect you with a consultant to help you through the process, sometimes at no cost to you.

Arizona Department of Transportation
Business Engagement & Compliance Office
DBE Supportive Services
1801 West Jefferson St., Ste. 101, MD 154A, Phoenix, AZ 85007
Phone: 602-712-7761

City of Phoenix
Community and Economic Development Dept.
Management Technical Assistance
200 W. Washington St., 20th Fl., Phoenix, AZ 85003-1611
Phone: 602-262-6007

Microbusiness Advancement Center
330 N. Commerce Park Loop, Ste. 160, Tucson, AZ 85745
Phone: 520-620-1241

Coconino Community College
Small Business Development Center
3000 N. 4th St., Flagstaff, AZ 86004
Phone: 928-526-7653

Coconino Community College
Small Business Development Center
475 S. Lake Powell Blvd., Page, AZ 86040
Phone: 928-645-6687

Maricopa Small Business Development Center
108 N. 40th St., South Building, Phoenix, AZ 85034
(and many other Valley locations)
Phone: 480-784-0590

TIPS FOR "CLEAN" FINANCIAL STATEMENTS

A company's success in obtaining financing or a bond depends largely on the business credit rating, condition of accounting records and owners' credit ratings.

Business Credit Rating

Like individuals, businesses have credit ratings. The primary business credit rating service for small business is Dun & Bradstreet (www.dnb.com). D&B assigns businesses a D-U-N-S number to track businesses (find or create your number at fedgov.dnb.com/webform). It bases its ratings on a variety of factors:

- › *Performance on past loans:* Make full payments on time every time. Lenders will report late payments to credit bureaus.
- › *Amount of borrowing compared to income:* Don't borrow more than the company can service with available income.
- › *Equity:* Keep profits in the business. If business owners put in more cash, show it as investment capital (increasing equity) rather than a loan (increasing liability).

Improve Business Performance

Business owners can act to improve the business' financial standing:

- *Cash is king:* Cash is the fuel that makes a business run. Reduce supplies inventory by delaying purchases until replenishment is actually needed. Eliminate non-essential expenses. Minimize payroll.

- *Manage accounts payable:* Pay all bills on time; suppliers may report late payments to credit agencies. Take advantage of early payment discounts, such as 2% if paid in 10 days (sometimes called "2% 10, net 30"); effective interest earning for a 20-days early payment is 36.5%!

- *Manage accounts receivable:* Write payment terms on proposals and invoices, including penalties and interest on late payments. Do *not* offer early payment discounts, such as "2% 10, net 30." Collect receivables within 30 days: email reminder notice at about 25 days after invoice; call two days later to ask about plans to pay the invoice; communicate regularly until accounts are paid in full. Do not do business with customers whose payment policy is more than 45 days after invoice.

- *Minimize overhead:* Rent fancy office space only for regular client meetings. Eliminate fax line by using a fax-to-email service. Cut fuel use by planning routes. Avoid credit cards with fees. Pay off credit cards monthly to avoid interest. Avoid late fees. Reward employees for money-saving ideas.

- *Allocate direct costs to contracts:* Direct labor, taxes and benefits; materials; major equipment hourly usage; performance bond; permits; rented equipment; supplies; subcontract costs; project travel based on logs; *etc.*

- *Include all costs in equipment direct costs,* including: depreciation; insurance; license; loan interest; oil and filters maintenance; repairs. Divide total annual costs by hours used per year to determine hourly usage rate.

- *Manage projects better:* Use inexpensive project management software to sequence tasks, assign tasks to "resources," estimate time required, record actual time spent, compare estimated cost to actual cost, and create invoices that can be exported to accounting software. (Compare at en.wikipedia.org/wiki/Comparison_of_project_management_software).

- *Manage projects for faster finish:* The faster a project is completed, the fewer overhead costs it will have to cover. The most profitable companies spend time planning and managing a project to get it completed quickly.

Personal Credit Score

Virtually all business loans require a personal guarantee by any owner of 20% or more of the business. Improving owners' credit scores will improve the business' ability to borrow capital.

Credit scores are determined by the three major credit reporting agencies: Equifax (www.equifax.com), Experian (www.experian.com) and TransUnion (www.transunion.com). These agencies use a secret formula called the FICO® score, which ranges from 300 to 850. A FICO score of 640 or higher is generally required for most loans, though some lenders require a higher score.

Improving the elements that make up the FICO score will make borrowing money easier:

- Payment history (35%): Make loan and credit card payments on time.

- Amounts owed (30%): Keep low amounts of loans and credit card debt, and low or moderate debt-to-credit limit ratios.

- Length of credit history (15%): Maintain a long history of borrowing money and paying it back timely.

- New credit (10%): Have few or no recently-opened credit accounts or credit history inquiries.

- Types of credit used (10%): Use a variety of different kinds of credit (mortgage, car loan, charge accounts, credit cards, *etc.*), rather than over-reliance on credit cards only.

Access a free credit report at www.annualcreditreport.com. After entering basic information, choose just one credit reporting agency. The law allows one free credit report from each agency each year. Monitor credit regularly with a free report from a different agency every four months.

A free credit report will not include a free FICO score. Learning your FICO score costs about $10. Knowing your FICO score is not necessary. If the credit report is clean, you will have a high FICO score; if it shows lots of exceptions or high debts, you have a low score.

The credit report lists all loans and credit accounts for several years, noting inquiries, late payments, closed accounts, defaults, repossessions and bankruptcies. The report may contain errors, such as: accounts belonging to family members or people with similar names; incorrect late payments; accounts opened by identity thieves.

If a credit report includes errors, start to correct them by calling the credit reporting agency; it may require you to contact the lender, who will write a correction letter. When one agency's information is corrected the others will automatically make the correction during the next few months.

INSURANCE

Businesses typically worry about six types of insurance:

- *Workers compensation* insurance pays workers' medical bills if they are injured on the job. Arizona requires every business to have workers compensation insurance if it has at least one employee other than the business owner. Rates depend on the industry and the company's safety record. The premium amount is the rate times the company's payroll.

- *General liability* insurance pays for any injury to a person other than an employee, such as if a pedestrian trips over a traffic barrier, or is misdirected by a flagger. It also may cover claims that exceed other policies' maximums. Rates depend on the industry, size of the business, the business' incident record and whether subcontractors are also covered.

- *Professional liability* insurance, also called "errors and omissions," pays for the results of mistakes by professionals such as engineers, architects, surveyors, accountants, consultants or others. Rates depend on the same factors as general liability.

- *Vehicle liability* insurance covers damage or injuries caused by motor vehicle accidents. It is required to license a vehicle in Arizona. Rates depend on the type and age the of vehicle and the driving records of authorized drivers.

- *Collision* insurance covers damage to the business' own motor vehicles caused by accident where an employee may be at fault. Collision insurance will be required by a lender financing the vehicle. Rates depend on the same factors as vehicle liability.

- *Property (fire and theft)* insurance protect a company's assets, such as buildings, vehicles and equipment. Rates are based on the value of the assets.

Businesses may also have employee group health coverage, and "key man" life insurance for owners and executives.

The health insurance industry is undergoing significant change as a result of implementing the Patient Protection and Affordable Care Act (ACA). Under this new law, businesses with fewer than 50 full-time-equivalent employees are *not* required to provide health insurance to their employees. Further, businesses with fewer than 25 full-time-equivalent employees may qualify for Small Business Health Care Tax Credits if they choose to help pay for employees' health insurance (see www.sba.gov/healthcare).

Businesses typically buy all their insurance from a single insurance broker. The broker will review the entire company and recommend a package of policies to address every need. Some brokers represent a single insurer, others are independent, representing many insurers. An independent broker may get multiple bids, and may recommend different insurers for different types of policies.

Insurers are rated by independent rating agencies based on their financial strength, credit and debt ratings. Customers may require that the insurer a company uses have a minimum rating, such as: "…an insurer with at least an "A" rating from A.M. Best Company." Most insurers are rated "A" or better. Other insurer rating companies include Demotech, Inc., Fitch, Inc., Moody's Investors Service, Standard and Poor's and Weiss Ratings.

TOP INSURANCE BROKERS IN ARIZONA

Arnett Insurance Services, Inc.
3850 E. Baseline Rd., Ste. 106
Mesa, AZ 85206
Phone: 408-830-7400
Brad Arnett

Beecher Carlson Insurance Agency, LLC
6970 E. Chauncey Lane, Ste. 100
Phoenix, AZ 85054
Phone: 888-996-7600
Frank A. Beranek

Bennett and Porter Insurance Services
3200 N. Hayden Rd., Ste. 310
Scottsdale, AZ 85251
Phone: 480-212-1150
Jack Bennett

Brown & Brown Insurance of Arizona, Inc.
2800 N. Central Ave., Ste. 1600
Phoenix, AZ 85004
Phone: 602-277-6672
John Esposito, Mike Paschke, Chris Scherzer

General Southwest Insurance Agency
5628 E. Thomas Rd.
Phoenix, AZ 85018
Phone: 480-990-1900
Joe Binsfeld, Dave Binsfeld

Hester, Heitel & Associates, Inc.
6122 N. 7th St.
Phoenix, AZ 85014
Phone: 602-230-7726
Mark Hester

Horizon Insurance Group, Inc.
2880 E. Northern Ave.
Phoenix, AZ 85028
Phone: 602-992-9750
James R. Mann

Hub International Insurance Services, Inc.
2375 E. Camelback Rd., Ste. 250
Phoenix, AZ 85016
Phone: 602-395-9111
Marc Meyer

LeBaron & Carroll, LLC
1350 E. Southern Ave.
Mesa, AZ 85204
Phone: 480-834-9315
Daniel Skinner

Lovitt & Touché, Inc.
1050 W. Washington St., Ste. 233
Tempe, AZ 85281
Phone: 602-956-2250
Charlie Touché

The Mahoney Group
1835 S. Extension Rd.
Mesa, AZ 85210
Phone: 480-730-4920
Glendon Nelson

Marsh and McCLennan Cos.
2325 E. Camelback Rd., Ste.600
Phoenix, AZ 85016
Phone: 602-522-6500
Cheryl Vogt

MassMutual Arizona
17550 N. Perimeter Dr., Ste. 450
Scottsdale, AZ 85255
Phone: 480-538-2900
Jeff Dollarhide

Minard-Ames Insurance Services, LLC
4646 E. Van Buren St., Ste. 200
Phoenix, AZ 85008
Phone: 602-273-1625
Steve Minard

NFP Property & Casualty Services, Inc.
8201 N. Hayden Rd.
Scottsdale, AZ 85258
Phone: 480-947-3556
Terrence Scali

Strunk Insurance Group, Inc.
14425 N. 7th St., Ste. 102
Phoenix, AZ 85022
Phone: 602-978-4414
Greg Strunk

USI Insurance
2201 E. Camelback Rd., Ste. 220A
Phoenix, AZ 85016
Phone: 602-279-5800
William Pilcher, II

Webb and Greer Insurance Agency, Inc.
301 W. Warner Rd., Ste. 113
Tempe, AZ 85284
Phone: 480-820-4040
Craig Webb

Wells Fargo Insurance Services USA, Inc.
100 W. Washington St., 4th Fl.
Phoenix, AZ 85003
Phone: 602-528-3000
Michael Taylor

Insurance brokers (also called producers/agents) and insurers are licensed by the Arizona Department of Insurance (www.azinsurance.gov). Verify a broker's ("producer's") license (az.gov/app/doilookup/ProfessionalSearch) and an insurer's license (az.gov/app/doilookup/InsurerSearch) on the Department's website. The Department's most recent *Annual Report* includes lists of all licensed insurers (including telephone number) and the top 25 insurers for different types of insurance (www.azinsurance.gov/annualreport.html).

BONDING

Many small businesses – particularly in the construction industry – may encounter three types of bonds:

- A license bond is required by a the Arizona Registrar of Contractors (ROC) as a condition of the license, in an amount ranging from $10,000 to $90,000 (www.azroc.gov/l_Bond.html). The bond is a guarantee that a licensed contractor will complete all projects in a workmanlike manner.

- A performance bond is typically required by customers and prime contractors, particularly in the construction industry. It is also a guarantee that the contractor will complete a project in a timely manner according to the plans and specifications and in a workmanlike manner, and pay all subcontractors timely.

- A bid bond is typically a letter from a bonding agent that certifies that the contractor will be able to get a performance bond if the contractor is awarded the project. Many bonding agents do not charge for issuing a bid bond, but it is an additional step in the bidding process.

A bond is a cross between an insurance policy and a loan. It is issued by a surety company.

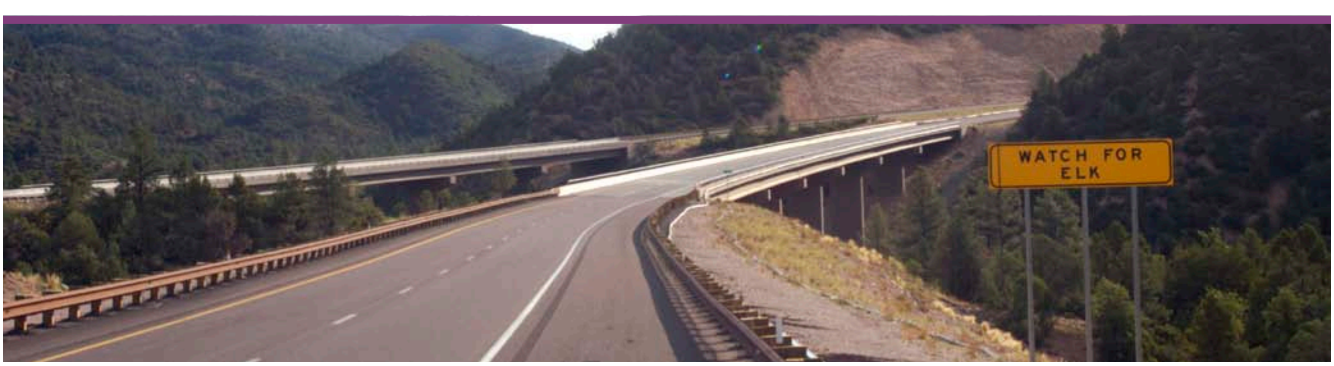
A dissatisfied customer may sue a contractor and, if successful, may file a claim to collect on the bond. The surety company will then pay the dissatisfied customer up to the amount of the bond. The surety company's payment creates a loan liability against the contractor, which the contractor will have to pay back with interest. The bond may include a personal guarantee as well.

Purchase a bond through a bonding agent. Some bonding agents only sell bonds, but many insurance brokers are also bonding agents. Applications will require the business' taxpayer identification number, and may require the principal owners' social security numbers.

A performance bond will require further information about the scope of work the contractor has committed to perform and a set of financial reports; some bonding companies may require the financial reports to have been audited or prepared by a CPA. The surety company wants to be sure the contractor has enough working capital to meet the contract requirements without running out of cash and losing its workforce. The surety company wants never to have to pay out a bond!

Because a bond can result in a loan, the key factors in being able to obtain a bond are the business' ability to complete the requirements of the contract, the company's credit rating and its owners' credit ratings.

The cost of the bond will depend on the amount of the bond, the industry, the business' performance history and financial strength and the owners' credit scores.



GLOSSARY

Adjustable rate – The interest rate on an adjustable rate loan changes at specified intervals (typically one, two or three years) based on changes in an underlying rate such as prime or LIBOR. See also "variable rate" and "floating rate."

Assets – Things that are owned. Assets may include: cash, bank accounts, certificates of deposit, stocks, bonds, tools, equipment, motor vehicles, homes, furnishings, real estate, and anything else of value that is owned.

Base interest rate – For SBA-guaranteed Basic 7(a) loans, either the (a) prime rate, (b) LIBOR one-month rate plus three percentage points or (c) SBA Peg Rate. For SBA-guaranteed CDC 504 loans, the current market rate for 5-year and 10-year U.S. Treasury bond issues.

Bond – See "surety."

Capital equipment – Equipment that typically costs $500 or more and is expected to last one year or more. Includes things such as backhoe, computer, generator, paver, transom, trailer, truck, *etc.*; would not include a shovel, rake, surveying stakes, hand tools, *etc.*

CDC – Certified Development Company – Nonprofit corporations certified and regulated by the SBA that work with participating lenders to provide financing to small businesses. Tucson has one and Phoenix has three, among 270 nationwide.

Collateral – Assets pledged by a borrower as a back-up to pay or service a loan; if the borrower fails to make required loan payments, including interest, the lender may seize the collateral and sell it to repay the loan. For an equipment or real estate loan, the collateral is the financed assets; for other loans, the borrower may have to pledge other collateral.

CPA – Certified Public Accountant, a professional certification.

Debenture – A certificate that certifies an amount of money owed to someone; a certificate of indebtedness. This definition describes an SBA-guaranteed CDC 504 loan.

Depreciation – The decline in value of an asset over time due to normal wear-and-tear and functional obsolescence. In accounting, depreciation is recorded as a non-cash expense on the Profit & Loss Statement, and as a reduction in both Assets and Equity on the Balance Sheet.

Debt service – The amount of principal and interest that must be paid on a loan every month, quarter or year.

Equity – The amount that business owners have invested in a company, plus all the previous profits the company has earned and kept in the business.

Factor – A type of business that buys accounts receivable at a discount, and typically has the payor pay the invoice directly to the factor.

Fees – Banks may charge borrowers fees to process and execute a loan. These fees may include legal fees, origination fees, processing fees, guarantee fees, points, and other charges.

Fixed rate – The interest rate on a fixed rate loan does not change over the life of the loan. See also "variable rate."

Floating rate – The interest rate on a floating rate loan changes any time the underlying standard interest rate, such as prime or LIBOR, changes. See also "adjustable rate" and "variable rate."

Guarantee fee – Government agencies charge a fee to provide banks a partial guarantee for the loan, and banks pass that fee along to borrowers; guarantee fees are based on the amount guaranteed, not the amount of the loan. Guarantee fees must be paid up-front, and may not be paid from the loan proceeds.

HUBZone – Historically Underutilized Business Zone – Specific geographical areas (zones) where small businesses in urban and rural communities can gain preferential access to federal procurement opportunities.

Interest – The cost of money; a percentage rate applied to the amount of a loan that the borrower must pay to the lender over and above the amount borrowed.

Legal fees – Banks may charge a fee to cover the cost of an attorney to review the loan documents. Legal fees are prohibited for SBA-guaranteed loans.

Liabilities – Things that are owed. Liabilities may include loans (both principal and interest), accounts payable and taxes owed.

LIBOR – The "**L**ondon **I**nter**b**ank **O**ffered **R**ate" is the rate of interest that big banks based in London, England, charge each other for short-term (one or a few days) loans; "LIBOR plus 3%" means the LIBOR rate plus three percentage points more, and is one of the three base interest rates banks may use on SBA-guaranteed loans.

Line of credit – A type of loan that lets borrowers draw funds as needed subject to a maximum loan amount, pay interest monthly and pay principal when the borrower wants; some lines of credit require a complete payoff at least once a year.

Loan-to-value ratio – The amount of a loan divided by the value of the asset that the loan is financing; for example: if a loan-to-value ratio of 80% is required for a $100,000 real estate purchase, the maximum amount of the loan is $80,000.

Maturity – The date by which a loan must be paid off; the end of a loan's term.

NAICS – North American Industrial Classification System; a standard code that shows what industry a business is in. Find a business' NAICS code at www.naics.com/search.htm.

Origination fees – Banks may charge borrowers a fee to pay a commission to a loan officer who brings the business to the bank. Origination fees may also include processing fees. Origination fees are prohibited for SBA-guaranteed loans.

Personal guarantee – If a business does not make required payments of principal and interest, a bank may ask the owners to make payments for the business; in some cases, a bank may sue and seize and sell personal assets owned by the business owners, such as bank accounts, stocks or bonds. Some types of property are exempt (protected) from such actions, but many are not.

Points – A fee paid to a lender in order to get a loan; points are typically expressed as a percentage of the loan amount. Points are usually charged to bring down the interest rate. For SBA-guaranteed loans, the guarantee fee may be called points. Points usually must be paid "up-front" before the loan documents are signed; borrowers often may not use the proceeds of a loan to pay the points. Points above the SBA guarantee fee are prohibited for SBA-guaranteed loans.

Prime contractor – The contractor that is awarded the contract for a project by the project owner. Subcontractors send their invoices to the prime contractor, who submits master invoices to the project owner, for example, the Arizona Department of Transportation. ADOT pays the prime contractor and then the prime contractor pays its subcontractors.

Prime rate – A rate of interest that banks charge their biggest and best customers; it is one of the three base interest rates banks may use on SBA-guaranteed loans.

Principal balance – The amount of a loan that is still unpaid, not including interest.

Principal owner – A person or another business that owns 20% or more of a business.

Principal – The amount of money borrowed or loaned, not including interest.

Proceeds – The amount of money borrowed, after deducting any fees.

Processing fees – Banks may charge a processing fee to cover the cost of preparing the loan agreement and other documents, legal fees paid to an attorney to review the loan documents and other fees. Processing fees beyond the SBA guarantee fee are not allowed for SBA-guaranteed loans.

Pro-forma – Latin for "as a matter of form." A *pro-forma* profit-and-loss statement (P&L) projection will be in the same form as a regular P&L, but will contain projected future amounts rather than actual past amounts.

Revolving – A type of loan that allows borrowers to pay down the loan periodically, then draw more funds as needed, subject to a maximum loan amount; see "line of credit."

SBA Peg Rate – A weighted average of rates the federal government pays for loans with maturities similar to the average SBA loan; it is one of the three base interest rates banks may use on SBA-guaranteed loans; it is calculated quarterly and published in the Federal Register (www.federalregister.gov).

Spread – A percentage amount added to a base interest rate to determine the total interest rate a borrower must pay; for example, a spread of 2.75% above a prime rate of 4.0% would result in a total interest rate of 6.75%.

Surety – A type of bond, issued by a surety company, through a bonding agent or an insurance broker. A bond is a guarantee that a contract will be fulfilled; if a contract is not fulfilled, the injured party may sue the contractor, and if successful, file a claim for the bond amount. The surety company will pay up to the bond amount, and create a loan for the contractor to repay the surety company.

Tangible balance sheet equity – A refinement of the accounting concept of "equity," in which normal equity is reduced by the assigned value of intangible assets, such as goodwill, going-concern value and organizational startup expenses. A CPA is generally required to document it.

Term – The length of time a borrower has to pay off a loan; the lifetime of the loan; the time between the loan and the maturity date.

Terms – Collectively, the conditions and provisions for a financial transaction such as a loan; terms might include: the amount of the loan; the interest rate; whether the interest rate is fixed, adjustable or floating; whether the borrower has to pay regular payments; the amount of any regular payments that may be required; the term, or time allowed to pay off the loan; any fees or points the borrower has to pay; *etc.*

Variable rate – An interest rate that is not fixed; a variable rate can be either "adjustable" or "floating."

Working capital – Money the business has on hand to pay for expenses, such as for inventory, labor and materials or overhead, before the revenue is received from the sale of the inventory or completion of a contract. The faster a company grows, the more working capital it will require.

Business Engagement and Compliance Office

DBE Supportive Services

1801 West Jefferson Street, Suite 101, Mail Drop 154A |
Phoenix, AZ 85007 Office (602) 712-7761 • Fax (602) 712-8429
www.azdot.gov/business/business-engagement-and-compliance