



Case Study: Providing Credit Solutions to Heavy Construction Contractors in Your Portfolio.

Lender	Borrower
Local community bank	Underground utilities company

Situation:

This case study provides a great example of how the lender-borrower relationship can grow successfully. Over time, each party better understands the needs of the other, and everyone gets a win. *Remember – you can conduct as many SBA loans as a small business borrower needs.*

An underground utilities company refinanced its business real estate with a new lender using an SBA 7(a) loan. Within a few months, the company needed a second 7(a) loan for additional equipment, a refinance of their existing equipment debt, and permanent working capital in order to increase bonding capacity. They approached their new lender with the request, which was for approximately \$1.6 million. The company was experiencing substantial growth and the second credit facility was necessary to enable the orderly expansion of sales.

By way of additional background, the contractor's clients are municipalities that let sewer and water projects, and require contractors to have a performance bond in order to be awarded projects. Bonding companies require permanent working capital in proportion to the size of the bond they issue. In order to increase bonding capacity to the size the contractor needed, the insurance company required an injection of \$300,000 in permanent working capital. Additionally, during the prior calendar year, the business incurred a rental of expense of \$400,000 by renting equipment necessary for the performance of its contracts.

The lender wanted to make this deal, but there were challenges. While this loan had good collateral, the liquidated value was insufficient to support the requested loan. The lender found itself wondering how to get this growing company the extra equipment and working capital it needed at a manageable debt service, so that the company didn't go out of business while trying to grow. The lender wanted this business to succeed – it was a profitable local company with experienced management that employed 15 to 20 people at above average wages.

Action:

Credit Facility: In 2015, the community bank turned to VITAL Financial Services for our expertise in underwriting, closing, and servicing SBA 7(a) loans. VITAL worked with the lender to provide a completely different approach to securing credit for the borrower. This included adding working capital to the term note -- not extending line of credit – and increasing the term of the loan to ensure strong cash flow for the borrower, which is critical for a business in its growth phase.

Using an SBA 7(a) term note, the bank was able to refinance the existing equipment debt, add the new equipment purchases to the refinance, provide the \$300,000 in permanent working capital required by the bonding company and pay expenses and closing costs. The lender was able to extend the term of the loan to 10 years – for the entire loan amount – to ensure the borrower had sufficient cash flow to repay the debt as agreed. **The total annual debt service was less than half what the company had previously paid annually just to rent its equipment.**

The required debt service for the term loan was small enough to be manageable, even while the company was in the midst of expanding. If the borrower performed well in future years, it could prepay the loan because there are no prepayment penalties on SBA notes under 15 years. The lender was able to give the business the requested amount of money regardless of the value of the underlying collateral. The 7(a) loan, while it takes all available collateral, does not limit the size of the loan to 75% of the market value of the assets. This allowed the bank to extend the needed funds for working capital and closing costs, even though there was no collateral backing that portion of the loan.

Risk Mitigation: VITAL worked with the lender to insure proper UCC lien searches, federal tax lien searches, and comprehensive business credit reports were obtained. VITAL made reports available to the lender for the borrower's industry metrics, which included industry default rates and recovery rates, comparisons to other companies in the same industry to check the borrower performance against peers, and provide assurance to the feasibility of the borrower's projections.

During the closing process, VITAL provided the lender with a comprehensive closing checklist, which outlined all the statutory requirements in the SBA loan authorization. This assisted the lender in obtaining all the necessary lien searches on business and personal assets. VITAL ensured that the loan proceeds used for refinancing the existing debt and purchasing the new equipment matched the Use of Proceeds in the loan authorization and obtained the SBA concurrence for any changes. VITAL assisted the lender in preparing a complete closing file in order to document that all requirements of the SBA Loan Authorization were met. A VITAL employee attended the closing to answer specific SBA questions and assist the bank in gathering the required documentation.

After the loan closing, VITAL prepares the monthly 1502 report and submits the report to Colson Services, assuring 100% accuracy. VITAL assists the bank with any loan modifications throughout the life of the loan by communicating with the SBA on the lender's behalf and insuring compliance with all applicable SOP's. If the requested modification falls within the Lenders Unilateral Authority, VITAL processes the changes through E-Tran.

Results:

The company has achieved its short-term sales growth objective while maintaining profitability and commitment to providing quality work. The bonding company increased the size of the bond it is willing to issue on the company's behalf. The risk of failure was reduced by the restructure of the existing debt and the injection of additional permanent working capital. Rather than simply extending more credit for new equipment purchases, the bank chose to work with VITAL to provide a more complete solution for the borrower.