Pennsylvania
Section 108
Loan Program

Standards for Financial Underwriting
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Section I – General Guidelines

A. Introduction

The PA Department of Community and Economic Development (DCED) has prepared guidelines for the Pennsylvania Section 108 Loan Program. As a part of this program, DCED has developed these “Standards for Financial Underwriting” for applications submitted for a Section 108 Loan.

These standards are applicable to all projects that are submitted to the Commonwealth of Pennsylvania either from non-federal CDBG entitlement communities on their own or through the PA Section 108 Loan Consortium. Non-federal CDBG entitlement communities are eligible to submit applications for Section 108 loans through the state where the community is located. Under the federal CDBG regulations, a state is responsible for choosing which public entities it will assist under the Section 108 Loan Guarantee Program. States are permitted to develop their own procedures and requirements for using Section 108 loan funds. Based on this, the Commonwealth of Pennsylvania prepared guidelines for the Section 108 Loan Program along with these financial underwriting standards. The “Standards for Financial Underwriting” have been developed to minimize loan loss exposure since the Commonwealth is providing an additional guarantee of up to 100% of the loan from state resources. This state guarantee is for development activities which have a cash flow or income source for loan repayment.

B. Section 108 Loan Program Summary

The PA Section 108 Loan Program has the following components outlined in the state guidelines:

1. Eligible Applicants:
   a. Members of the PA Section 108 Loan Consortium
   b. State CDBG entitlement public entities applying on their own

2. Non-eligible Applicants:
   a. Federal CDBG entitlement communities
   b. Urban counties receiving CDBG funds
   c. Municipalities that have opted into an urban county.

3. Eligible Activities:
   a. Economic Development Activities:
      • Acquisition, construction, reconstruction, rehabilitation or installation of commercial or industrial buildings, structures, and other real property.
      • Machinery and equipment.
      • Infrastructure, including railroad spurs.
      • Assistance to a private for-profit business: loans, loan guarantees, interest supplements, technical assistance and other forms of support.
      • Activities under taken by a community-based development organization (CBDO).
   b. Housing Activities:
      • Rehabilitation of privately owned buildings and improvements
      • Rehabilitation of low-income public housing
• Rehabilitation of other publicly owned residential buildings
• Construction of housing by non-profit organizations for homeownership

c. **Community Development Activities:**

• Acquisition, construction, reconstruction, rehabilitation, or installation of public facilities (except for buildings for the general conduct of government), public streets, sidewalks, and other site improvements, and public utilities
• Acquisition of improved or unimproved real property in fee or by long-term lease
• Rehabilitation of real property owned or acquired by the public entity or its designated public agency
• Relocation payments and other relocation assistance for individuals, families, businesses, non-profit organizations, and farm operations who must relocate permanently or temporarily as a result of an activity financed with Section 108 loan funds
• Clearance, demolition and removal, including movement of structures to other sites; or buildings and improvements on real property acquired or to be rehabilitated
• Site preparation, including construction, reconstruction, or installation of public and other site improvements, utilities, or facilities which are related to the redevelopment or use of real property acquired or to be rehabilitated, or for an economic development purpose

d. **Other Eligible Costs:**

• Payment of interest on obligations guaranteed under Section 108
• Payment of issuance, underwriting, servicing, trust administration and other costs associated with private sector financing of debt obligations
• Operating reserve fund to insure continued occupancy and maintenance.
• A debt service reserve to be used in accordance with a requirement specified in the contract for a Section 108 loan

4. **Priorities:**

Section 108 loan funds will be made available for economic development, community development, and housing activities. The following priorities should be considered in evaluating a Section 108 loan application.

a. **Job Creation:** minimum of one permanent full-time job equivalent (FTJE) must be created for every $35,000 of Section 108 loan funds used for economic development activities.

b. **Low- and Moderate-Income Benefit:** proposed activities should principally benefit low- and moderate-income persons. However, worthwhile projects that aid in the prevention or elimination of slums and blight should also be considered.

c. **Infrastructure Improvements:** the installation, construction or reconstruction of critical infrastructure that will correct or address a public health and safety problem.

d. **Special Economic Development:** financial assistance to a private for-profit business that is eligible under the CDBG guidelines, provided the activity principally benefits low- and moderate-income persons.

e. **Housing:** rehabilitation of existing housing and/or the construction of new housing by non-profit organizations for homeownership, provided that the housing is affordable to low-and moderate-income persons.
C. Projects Eligible for Section 108 Loans

Communities participating in the PA Section 108 Loan Consortium may apply for any of the following categories of eligible projects. Each one of the following three general categories have specific project types that are eligible for Section 108 financial assistance.

1. Economic Development Projects:
   Examples of economic development projects include loans made by the public entity to a for-profit business, development of a business or industrial park, construction or reconstruction of infrastructure to support a business, or implementation of a redevelopment project.
   
a. Business Loans – funding provided to a local firm for expansion of its operations. Funds may be used for construction, purchase of machinery and equipment, gap financing, as a credit enhancement, etc. A project of this type would normally include other sources of funding and capital invested by the company. The project must create new job opportunities which would be made available to low- and moderate-income persons. The Section 108 loan would be repaid by the company from cash flow from the increase in revenue from operations.

b. Business/Industrial Park – funding provided to purchase improved or unimproved real estate for the development of a business or industrial park. The project would make sites available for companies to purchase and locate their operations at that site. The project should create new job opportunities which would be made available to low- and moderate-income persons. The Section 108 loan would be repaid from the sale of land to private firms and from lease or rental income.

c. Infrastructure Improvements – for the construction or reconstruction of access roads, the extension of public utilities, installation of a railroad spur line, etc. to serve a private business or industry. The project should create new job opportunities which would be made available to low- and moderate-income persons. The Section 108 loan would be repaid by the company from cash flow from the increase in revenue from operations.

d. Redevelopment Project – funds would be used for the acquisition, relocation, rehabilitation of buildings, and clearance of site(s) for redevelopment purposes. The land would be sold to public or private redevelopers and the funds from the sale of the land would be used to pay off the Section 108 loan, along with supplemental funding such as tax incremental financing (T.I.F.), CDBG annual allocations, etc. The project must benefit low- and moderate-income persons through the creation of new job opportunities.

2. Housing Projects:
   Examples of housing projects that are eligible for Section 108 loans include rehabilitation, acquisition of sites for new development, homeownership, etc. All housing type activities must be affordable to low- and moderate-income persons.
   
a. Bridge Loans – funds may be used to provide interim financing for construction of single family or multi-family residential units for homeownership or as rental housing, by a non-profit housing organization. Sources of permanent financing could be through a state housing development agency, low-income housing tax credits, or private banks. The Section 108 loan could be used as a “bridge” loan for construction financing. Repayment of the Section 108 loan would be made at the time when the permanent financing is in place, such as from sales of individual houses.

b. Housing Rehabilitation – funds may be used to establish a loan pool for homeowners or landlords to borrow from at low interest rates with long term repayment terms. The homeowners or tenants must be low- to moderate-income. Repayment of the Section 108 loan could be from the individual monthly loan repayments by the homeowners/landlords and could be supplemented with CDBG funds on an annual basis.
c. **Homeownership** – funds could be used to establish a first time homebuyer program for down payment assistance or mortgages at favorable interest rates and repaid over a twenty year period. The development of the housing would be done by a non-profit housing agency and the houses would be sold to low- and moderate-income families. Repayment would be from the homebuyers which could be supplemented with CDBG funds.

3. **Community Development:**
Large scale public facilities and infrastructure type projects may be undertaken with Section 108 loan funds. These projects may be beyond the annual CDBG budget limitations of communities. These projects must benefit the low- and moderate-income population of the area in which they are intended to serve.

a. **Water and Sewer** – funds may be used to construct, reconstruct, or expand water and sewer lines to serve low- and moderate-income areas of the community. Repayment of the Section 108 loan could be from long term user fees for the lines, general revenue funds, or from annual CDBG allocations.

b. **Storm Water** – funds may be used to construct, reconstruct, or expand storm sewer lines to the low- and moderate-income areas of a community. These types of projects are often difficult to finance with other sources of funds. Repayment of the Section 108 loan would most likely have to be from multiple sources such as sewer fees, general revenue, or from annual CDBG allocations.

c. **Parks and Recreation** – funds may be used for the expansion of an existing park facility or the development of a new facility. The facility must principally benefit low- and moderate-income persons. Repayment of the Section 108 loan could be from CDBG funds or general revenue funds.

d. **Streetscape Improvements** – funds may be used to provide loans/grants for building façade improvements, streetscape work such as tree planting, walks, curbs, street furniture, signage, street reconstruction, etc. The area must serve principally low- and moderate-income persons, or be part of a redevelopment project to prevent or eliminate slums and blight. Section 108 loan repayment could be from annual CDBG allocations, or a special tax levy on the property owners through the establishment of a neighborhood improvement district or a business improvement district (B.I.D.).

e. **Infrastructure Improvements** – for the construction or reconstruction of roads, streets and public utilities. The activity would be located in low/mod income area. Repayment of the Section 108 Loan could be from CDBG funds or general revenue.

f. **Public Facilities** – funds maybe used for purchase, rehabilitation on construction of public facilities which principally benefit low/mod income persons. Repayment of Section 108 Loan would be from CDBG funds.

**D. Overview of Standards**
The Pennsylvania Department of Community and Economic Development (DCED) has developed these standards to provide the members of the Section 108 Loan Consortium and other eligible participants in the Section 108 Loan Program with a framework for financially underwriting and evaluating the eligibility of potential projects for Section 108 loan financing. The HUD Section 108 Loan Program requires that state or public entities must conduct basic financial underwriting prior to approval of a Section 108 loan.

These standards recognize the three (3) basic categories of Section 108 loans and the inherent differences in each type. In addition, the size and scope of certain proposed projects also will dictate the level of review required. In particular, smaller economic development loans to a micro-enterprise or another small business must take into account the differences in capacity and level of sophistication among businesses of differing sizes.
1. **Objectives of Financial Review:**

The objectives of the financial review of each application are the same as the HUD *Guidelines and Objectives for Evaluating Project Costs and Financial Requirements* that are found in Appendix A to Part 570 of the Federal Regulations. These objectives are to ensure:

- that the project costs are reasonable;
- that all sources of project funding are committed;
- that to the extent practicable, Section 108 funds are not substituted for non-federal financial support;
- that the project is financially feasible;
- that to the extent practicable, the return on the owner’s equity investment will not be unreasonably high (in the case of a loan to a private firm); and
- that to the extent practicable, the Section 108 loan funds are disbursed on a proportional basis with other finances provided to the project.

2. **Additional Standards:**

DCED will also be evaluating the following criteria in its project review:

- is the project feasible and is it supported by market studies, engineering studies, housing studies, feasibility studies, etc.;
- is the project site/location suitable for this project;
- what is the capacity and capability of the project development team;
- does the project meet the eligibility criteria of the Section 108 loan program;
- what is the public benefit to be derived from the project; and
- what are the sources of loan repayment.

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**Section II – Underwriting Standards & Guidelines**

**A. General Loan Parameters**

The DCED Standards for Financial Underwriting will comply with the Federal Regulations for the use of Section 108 loan funds and will take into consideration the following factors listed in the “Overview of Standards” found on Page 5 of this document.

1. **Project Costs Are Reasonable:**

   All project costs will be carefully reviewed for reasonableness. A breakdown of all project costs will be required for the Section 108 loan application. Fair market price quotations, engineer’s estimates, appraisals, etc. must be submitted to support all project cost elements. Third party price quotations are required to verify costs. Non-arms-length or in-house quotations will not be accepted.

   A “sources and uses of funds” form will be reviewed for each “use of funds” (cost element) and a determination will be made on the reasonableness of the cost.

   - for construction, machinery and equipment costs, costs will be reviewed based on estimates from the third-party contracts (architect, engineer, equipment supplier, installer, etc.)
   - for land/building acquisition, a determination will be made that the price is reasonable based upon the fair market value by a certified real estate appraiser.
c. for development costs (building fees, architectural/engineering fees, financing fees, etc.) a determination be made if the costs are itemized and supported by contracts or other documentation.

d. for working capital (if applicable), a comparison will be made on the amount of working capital requested as compared to industry averages, risk, historical needs of the business and the projected need. This will be accomplished by analyzing the financial statements, projections, operating cycle and financial ratios.

2. **All Sources of Project Financing Are Committed:**
A review will be made to determine if sufficient sources of funds have been identified and are committed to the project. The participating financing parties have the financial capacity to provide the funds in a timely manner. The terms and conditions of the other sources of funding must be disclosed.

A “sources and uses of funds” form will be reviewed for all sources of funds. A determination will be made if there is evidence verifying the commitment or an intent to commit funds.

a. for debt (loan) sources, letters of intent or interest must be provided with the specific level of commitment and the terms and conditions of the loan.

b. for debt (loan) sources, provide copies of the actual loan package that was submitted to the lender.

c. for grant sources, letters of commitment must be provided which outlines the level of commitment, any commitment, any conditions and the timing for receipt of the funds.

d. for equity (cash) sources, a determination will be made if the equity can be verified by business or personal bank financial statements. If the equity is to be provided by an outside investor, evidence must be obtained on the level of commitment, the terms and conditions if any, availability of funds, and an accompanying financial statement verifying the availability of the funds.

3. **Section 108 Loans Are Not Substituted for Non-Federal Funds:**
The amounts and sources of funds will be reviewed to ensure that Section 108 loan funds are not being used to substantially reduce the amount of non-federal funding for the project.

In order to receive a Section 108 loan a project must have a “financial gap.” This gap must be documented. There are three (3) types of financial gaps.

a. **Unavailability of Capital.** The project can afford the cost of financing, but is unable to obtain the funds from private debt and/or equity sources. The gap may be a result of a lender’s loan to value requirements or the inherent risk of the project or the industry. For example: a loan is provided for 70% of the project’s cost, which leaves a 30% financing gap. The business may not have the cash to “bridge” the gap, or its cash flow would be seriously restricted and it could jeopardize the business. Other lending sources, both public and private, need to be explored.

b. **Cost of Capital.** The project cannot support the interest rate, the loan term, and/or the collateral requirements of the lender. To analyze this gap, a determination has to be made to determine if the lender is willing to change its terms. The gap may only be a problem in the initial years of the project. A pro forma, cash flow, needs to be reviewed with several scenarios which would defer principal and/or interest, or to allow the loan to be amortized over a longer period.

c. **Return on Equity Investment.** The project’s financial returns may be too low to justify the business or a third party investor to proceed with the project. The risks of the project outweigh the returns. The rate of return on investment must be reviewed and adjusted to industry standards, as well as location risks, to determine if the gap does exist. The Section 108 loan rate and term can be designed to provide a return that is in line with similar projects. This may not apply to non-profit organizations.
4. **The Project is Financially Feasible:**
The project will be examined to determine its viability and assure that the public benefit will be realized. The current and historical financial statements of both the business and principals will be analyzed. Income and expense costs shall be evaluated and compared historically. The income and expenses will be compared to industry averages. Project costs will be reviewed to determine their reasonableness.

As a part of this financial analysis, the past, current, and projected financial data will be analyzed to determine if the job estimates are reasonable and can be supported. Labor costs shall be checked against industry averages.

The terms and conditions of the Section 108 loan must be appropriate. The interest rate should be set at a rate where available cash flow is able to meet debt obligations with enough remaining cash flow to operate successfully. The loan term will be based on the asset being financed. The term will not exceed the economic life of the asset being financed or twenty (20) years as established by the Section 108 Program Guidelines. A longer loan amortization schedule may be justified with the loan due at the end of the economic life of the asset. Each loan will include a written explanation of this appropriate analysis and the reason for recommending the loan terms and conditions.

5. **The Return on Equity Investment is Reasonable:**
The Section 108 loan application will be reviewed to determine if the return on investment to the business owner is reasonable. The amount of cash that the investor/owner is projected to receive, in relation to their initial equity, will not unduly enrich them. However, the analysis will also take into consideration if the return on investment is too low, which could cause the investor/owner to lose motivation and not follow through with the project.

A review will be made of projected revenues, expenses (including owners’ and officer’s salaries), owners’ draws, debt service and net operating income. A comparison to historical financial information will be made in relation to industry averages to determine reasonableness.

A review of the business’ and personal obligations will be made to determine what return on equity investment is necessary to meet personal and business obligations. If the return on investment is above the industry averages, adjusted for risk and local conditions, steps will be taken to adjust the Section 108 loan terms or reducing owners'/officers’ salaries and/or draws. If the return on investment is below the industry average, the loan terms may be adjusting to bring it closer to the industry average.

6. **The Section 108 Loan Funds will be Disbursed on a Proportional Basis:**
To the extent practicable, the Section 108 loan funds should be disbursed on a pro rata basis with other funding sources to avoid placing the Section 108 Loan funds at a greater risk than other funding sources, since the Section 108 funds would be spent before the other funding sources are used.

The sources and uses of funds will be reviewed to determine if the Section 108 loan funds will be expended at the same ratio as the other funds. A review of the other funding sources’ policies on the expenditure of funds will be made. If these policies require the public funds to be disbursed first, negotiations will be made to review these policies. If the Section 108 funds still will be expended first, safeguards such as performance or completion bonds should be considered.

7. **The Public Benefit Will be Achieved:**
Each project be reviewed to determine if the minimum level of public benefit will be realized for the expenditure of Section 108 loan funds. The minimum standards are:

a. For each $35,000 of Section 108 loan funds, there must be the creation or retention of at least one full-time equivalent job (FTEJ), or
b. The project will provide goods or services to residents of an area, such that the number of low- and moderate-income persons residing in the area served by the business amounts to at least one low- and moderate-income person per each $350 of Section 108 loan funds.

A review of the historical financial statements will be made in regard to labor costs as a percentage of revenue. A comparison of the percentage of projected labor costs will determine if the projected labor figures are consistent with the project’s revenue. The labor costs will also be evaluated to industry averages. The assumptions used to project revenue and labor costs must be supported by market/industry information and historical financial statements.

8. **The Project Is Feasible:**
In addition to the financial feasibility of a project, an analysis will also be made on the feasibility of the development. The Section 108 loan application must be supported with additional documentation such as:

- Market studies
- Real estate appraisals
- Engineering studies
- Housing studies
- Feasibility studies, etc.

These reports must be prepared by a third party source which has the qualifications to perform the study. In-house or subsidiary vendors will not be considered since this is not an arms-length transaction.

These studies are especially important in evaluating housing projects and community development activities. Where there is not a revenue source produced by the project, the need for engineering and other types of feasibility studies are necessary to properly evaluate a project.

9. **The Site and Location Are Suitable:**
The project site and its location will also be evaluated for each Section 108 loan application. The following factors will be reviewed to determine the suitability of the project in relation to its environment.

a. The neighborhood where the project is located should show signs of stability with strong and continuous growth patterns. In the case of a redevelopment area, the proposed redevelopment area plan must be sufficiently designed and funded to achieve the anticipated outcomes.

b. The property’s condition is important, both structurally and environmentally. Third party studies and reports will be analyzed such as: a property appraisal, Phase I Environmental Site Assessment, property condition assessment, and, if necessary, an operations and maintenance program for removal of asbestos, lead-based paint, radon, PCB’s, other toxic waste, and the removal of underground storage tasks.

c. An evaluation must be made in regard to adequate zoning. A statement from the community zoning officer must state that the proposed use of the site is classified as either a legal conforming or a legal non-conforming use under local zoning requirements.

d. Proof of ownership and proper title to the property must be evident.

e. A survey of the property from a licensed land surveyor showing meets and bounds, a written legal description; easements, encumbrances, rights-of-way, physical features, utility lines, etc. will be reviewed.
10. **The Development Team Has the Capacity and Capability to Undertake the Project.**
   A written description of the development team will be evaluated. This description will outline roles and responsibilities and provide previous experience in similar types developments. This will be supplemented with resumes and historical backgrounds.

11. **The Project Meets the Eligibility Criteria:**
    The project will be evaluated in accordance with the HUD Guidelines found in 24 CFR Sub-Part M, 570.703 Eligible Activities. The project must be eligible under one or more of these thirteen (13) listed activities of the HUD Guidelines for Section 108 loan guarantees. In addition, for those applications submitted through the PA Section 108 Loan Consortium, the application must be for one of the eligible type projects.

12. **Public Benefit Will be Derived:**
    The project must meet the HUD Public Benefit test as found in the HUD Guidelines in 24 CFR Sub-Part C, 570.209 (b) Standards for Evaluating Public Benefit. The standards for economic development loans must meet the following criteria:
    
    a. Create or retain at least one full-time equivalent, permanent job per $35,000 of CDBG funds used; or
    
    b. Provide goods or services to residents of an area, such that the number of low- and moderate-income persons residing in the areas served by the assisted businesses amounts to at least one low- and moderate-income per $350 of CDBG funds used.

    In addition, all activities funded with Section 108 loan funds will be evaluated in accordance with the Criteria for National Objectives found in the HUD Guidelines under 24 CFR Sub-Part C, 570.208. These criteria include:
    
    
    b. Activities which aid in the prevention or elimination of slums or blights, or
    
    c. Activities designed to meet community development needs having a particular urgency.

    All proposed Section 108 activities must meet one of these three (3) National Objectives. Traditionally, economic development activities have to create or retain jobs for low- and moderate-income persons, but other types of Section 108 loans must also, meet an objective such as undertaking an activity that benefits located in a predominantly low- and moderate income persons.

13. **The Loan Will Be Repaid:**
    All Section 108 loans must be repaid. Not all proposed activities have cash flow to repay the loan. Therefore, other sources of funds will be evaluated to determine the capacity to repay the loan. For economic development loans, cash flow must be sufficient to meet debt service. The goal for the cash flow coverage ratio or debt coverage ratio should be 1.25 to 1.00, which means $1.25 in cash flow is available for every $1.00 in debt service. Additional sources of cash flow will be required for a business that has a cash flow coverage ratio of less than 1 to 1. This may include a cash reserve account for debt service from the owner or an investor, and a cash equivalent resource, such as a certificate of deposit.

    For community development type loans other sources of funds for repayment will be reviewed and evaluated, such as:
    
    a. increase in property taxes (i.e. tax incremental financing, T.I.F.)
    
    b. revenues derived from the project (i.e. lease payments, rental payments, or parking revenue, etc.)
    
    c. user fees (i.e. water or sewer fees), etc.
B. Borrower & Key Principals

1. **Borrower:**
The borrower of the Section 108 loan may be a public entity, a designated public agency, a non-profit corporation, or a private single purpose entity. An evaluation of the borrower’s capacity and capability will be made.

In the case of a private single purpose entity, allowable ownership may be individual(s), general or limited partnerships, corporations, and limited liability companies.

The borrower must be creditworthy and support that with accountant prepared financial statements. This includes both private and public entities.

2. **Key Principals:**
In the event the borrower is not an individual, the key principals of the borrower must be identified. A “key principal” is a person who is critical to the successful operation and management of the business. A review of the company’s organizational documents will be made to determine the appropriate person(s) to designate as a key principal. A thorough credit review will be made for each key principal.

Key principals must have financial capacity and relevant experience as demonstrated by resumes and financial statements. Credit checks and full background disclosure will be required on all individuals or entities owning or controlling twenty percent (20%) or greater interest in the company.

Key principals will collectively have the obligation to guarantee one hundred percent (100%) of the loan’s principal balance.

3. **Financials:**
The borrower’s and key principal’s overall financial strength, as well as their previous history of ownership and successful operation of a business will be considered. At a minimum the following documentation must be provided:

a. Credit reports for the borrower and key principals
b. Verification of employment for individual borrowers
c. Federal income tax returns for the two previous years for the borrower
d. Bank statements for the borrower for the most recent three (3) months
e. A current balance sheet identifying contingent liabilities for the borrower
f. A current income and expense statement for the borrower
g. A detailed schedule of other real estate holdings of the borrower
h. Proof of ownership and loan statement which describes any bankruptcy which occurred within the last seven (7) years and any pending or current litigation or judgments.
Section III – Financial Analysis

A. Financial Statements

These financial analysis concepts and guidelines should be applied to the analysis of both corporate and personal financial statements when appropriate.

1. Understanding the Financial Statements:

   Financial statements are the basic method of measuring the performance of a business. They include a balance sheet, income statement and statement of cash flow.

   a. The balance sheet shows what a company owns and owes.

   b. The income statement shows a company's sales, expenses and profits.

   c. The cash flow statement shows a company's ability to generate and manage cash.

Not all businesses will prepare all the statements. Some sole proprietors do not prepare balance sheets. There are many businesses that do not prepare cash flow statements. For the purposes of performing financial statement analysis, at a minimum, the last three-year's income statements and a current balance sheet and income statement are required.

It is necessary to know the accounting method the company is using.

   a. **Accrual Accounting:** Is a measure of a company's earning activities. In accrual accounting, a sale made on terms, but not collected, is still accounted as a sale. Likewise, an expense is booked when it occurs, even if paid later. With accrual based accounting, it is important to get the balance sheet so that you can analyze how well the company is collecting from its customers and paying its suppliers.

   b. **Cash Accounting:** Is a measure of a company's cash generating activities. It is also called "checkbook" accounting because a sale is recorded only when the payment is collected and expenses are recorded only when the payment is actually made. A balance sheet that is prepared on a cash basis will not have accounts and notes receivables, accounts and notes payables or accruals. Many businesses that prepare financial statements using cash basis accounting will make sales on terms and take terms from their suppliers. It is therefore important to request information on receivables and payables.

   Cash accounting understates the real profitability of a company and makes it hard to determine working capital position and needs.

   Some companies prepare financial statements in house on a monthly basis. This practice is an indication that management is utilizing this information to financially manage day to-day operations. This becomes increasingly important to a company that is growing and critical to a company that is on a fast growth track.

   A company that has its accountant prepare only a year end financial statement may not have any idea as to the financial condition of the company except at one time during the year. If a company does not prepare monthly statements, questions must be raised about the financial statements. In particular, information must be provided about profit margins, accounts receivable, or inventory turnover. This will help determine whether owners are adequately managing the financial aspects of their company.
There are three levels of accountant prepared financial statements:

- **Audited:** The CPA evaluates all aspects of the business from counting the inventory to verifying debt and everything in between. An "opinion" is then issued stating whether the borrower has followed generally accepted accounting principals in the financial accounting of its business. A "clean" opinion indicates that the business has done so. A "qualified" opinion means that the accountant believes there is something serious enough to prevent them from issuing a clean opinion. The problem must be stated within the text of the opinion. If the opinion is "qualified" discuss the situation with the owner(s), the situation and your discussions will become part of your analysis. Audited financial statements are the most costly to a business owner.

  An explanation of the “qualified” opinion must be part of the Local Originator/Underwriter’s risk analysis.

- **Reviewed:** The CPA reviews information provided by the business and provides limited verification, along with doing some key "tests" to validate levels of inventory and receivables.

- **Compiled:** The CPA uses the information provided by the business and puts it in the proper form. The accountant does no evaluation as to the correctness or completeness of information.

Should a business not have audited, reviewed or financial statements compiled by a CPA, financial statements compiled by the company will be accepted as long as they are generated from a proper general ledger based accounting system. As a last resort, the company’s income tax returns may be utilized. Submission of the financial statements with the highest degree of integrity possible is recommended.

In preparing the draft Loan Commitment, the Local Originator/Underwriter must determine the quality and the frequency of financial statements the business will need to send the Lender on an on going basis for servicing the loan. A good rule of thumb to follow is this: whatever quality of financial statement used for approval of the loan should be sufficient on an on-going basis.

The Section 108 Loan Program requires the best possible financial statements available on a quarterly basis and CPA Reviewed financial statements on a an annual basis, along with the receipt of Federal income tax returns for the Borrower entity annually.

2. **Preparation of Financial Statement Analysis Spread Sheets:**
   Financial statements should be entered onto a financial spreadsheet in standardized format. See Addendum for Financial Statement Spread Sheet templates. The Local Originator/Underwriter will transfer the numbers from the balance sheet and income statement for the last three years, the current period and projected financial statements, if applicable. These “spread” statements will need to be compared to industry standards for the SIC Code of the business.

   Comparative industry statistical information is available from Moody’s. Other industry sources may include:

   - Dun & Bradstreet's Industry Ratios
   - Trade Associations or Trade Publications
   - U.S. Commerce Department Industry Analysis

   The financial spreadsheet will be used to evaluate the historical performance of the company and its ability to repay the proposed loan. Remember to be consistent in categorizing items across financial statements and spread "like kind" financial statements, i.e., all tax returns or all financial statements.
Once all the financial statements are entered on the spreadsheet, the Local Originator/Underwriter will begin its analysis. A more mature company with stable historical financial performance will require far less discussion in the credit analysis than a company that is less stable such as a young company or one that shows inconsistent historical performance.

3. **Ratio Analysis:**

   Ratio analysis is a shortcut method of asking key questions about the financial performance of the business. Each ratio uses information from the financial statements to quantify the ability of the business to generate sales, control costs and manage cash. Ratio analysis is a tool to assist in the identification of questions to ask.

   Ratio analysis is the primary method used by banks and other grantors of business credit.

   Ratio analysis is the process of analyzing:

   a. Trends of the business over time
   b. Comparison with industry
   c. Comparison with the business' desired operational goals
   d. Questions to be answered

   Ratio analysis uses common size statements. Financial statements on spreadsheets are converted from dollar amounts to percentages to make comparisons over time.

   a. **Balance Sheet Ratios:** compares current assets, other assets and fixed assets as a percentage of Total Assets. Also, compares current liabilities, long term liabilities and equity accounts as a percentage of Total Liabilities and Equity. Asset accounts can also be compared to liability accounts (current ratio), while liability accounts can be compared to equity accounts (debt to asset ratio).

   b. **Income Statement Ratios:** numbers are analyzed as a percentage (%) of Sales

   Moody’s financial ratios are the most commonly used ratios to compare businesses with their industry. Moody’s collects financial statements from a number of businesses in a large number of industries according to The North American Industry Classification System (NAICS). It then calculates a range of financial ratios for comparison purposes.

   **To use Moody’s ratios effectively requires the following:**

   a. Select the proper NAICS code for the business being analyzed. This may be difficult. Some businesses don’t know their NAICS code. This may be determined through NAIC resource material. Furthermore, companies commonly do business in several NAIC codes. Select the one that coincides with the largest part of a business’ activity (sales). If there is not a good "fit" with the only available NAIC code, make the comparison but then annotate that the comparison is not a good one and why.

   b. Select the proper sales category for the business. Select the sales level that is closest to the current sales for the company. If the company has recently gone into a higher category, consider using the lower category

   c. The ratios are organized similar to a Balance Sheet and Income Statement

   d. Some of the ratios, particularly those concerning the operating cycle, provide a range of ratios, reflecting best and worst case situations. These are call "lower quartile" for the lower 25% performing businesses, "median" for the middle 50% of the businesses, and "upper quartile" for the top 25% of the businesses with the highest performance in their industry.
4. **The Balance Sheet:**

The Balance Sheet is a snapshot of a company's resources at one point in time. It is comprised of assets, liabilities and net worth.

\[ \text{Total Assets} = \text{Total Liabilities} + \text{Total Net Worth} \]

<table>
<thead>
<tr>
<th>Balance Sheet</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>as of 00/00/00</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Assets</th>
<th>Liabilities &amp; Net Worth</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Assets</td>
<td>Current Liabilities</td>
</tr>
<tr>
<td>Long-term Assets</td>
<td>Long-term Liabilities</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td></td>
</tr>
<tr>
<td>Total Net Worth</td>
<td></td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td><strong>Total Liabilities &amp; Net Worth</strong></td>
</tr>
</tbody>
</table>

**Assets:**

**Current Assets:**

- Are used in day to day operations,
- Can be converted into cash within 12 months; and
- Normally listed in the order of how quickly each can be converted to cash.

**Current Assets include:**

- Cash on hand, in the bank and marketable securities,
- Accounts Receivable – amount listed is net of any allowance for uncollectible accounts,
- Inventory – includes raw materials, work in progress, finished goods,
- Prepaid Expenses – such as prepaid rent, insurance, employee advances (prepaid wages); and
- Other Current Assets – such as tax refunds, funds deposited but uncollected, notes receivable portion collectable within 12 months.

**Long term Assets are:**

- economic resources that have a longer life than 12 months,
- generally not used for day to day cash needs of the company; and
- needed longer term to manufacture, display, warehouse and transport goods sold by the company to generate sales.
Long-term Assets include:

- Net Fixed Assets – such as land, building, machinery and equipment (net of any accumulated depreciation),
- Notes Receivable – collectable after 12 months,
- Investment in or advances to subsidiaries,
- Intangibles – such as good will, patents, copyrights, research & development, and organization expenses (net of amortization); and
- Other Fixed Assets – such as long term deposits.

Liabilities

Current Liabilities are:

- Sources of cash for operations; and
- Must be repaid within 12 months or an organization’s operating cycle (which ever is larger).

Current Liabilities include:

- Notes Payable to Bank – typically the line of credit,
- Notes Payable to Others – typically notes to suppliers,
- Accounts Payable – money owed to suppliers,
- Accruals – payroll taxes, wages, interest expenses due but not yet paid as of date of the balance sheet,
- Income Tax Payable – Federal and State,
- Current Portion Long Term Debt – principal portion of long term debt due within 12 months; and
- Other Current Liabilities – such as loan from officers not subordinated and due within 12 months, current portion of capitalized leases.

Long-term Liabilities are:

- Principal portion of debt not due within 12 months; and
- Generally purchase of fixed assets or permanent working capital.

Long-term Liabilities include:

- Long term Debt – principal portion of debt due longer than 12 months including capitalized leases; and
- Subordinated Officer Debt – money loaned to the company by officers.

Net Worth

Net Worth represents the value of the company's resources provided by the owners of the business.

Net Worth includes:

- Common Stock – value of the purchased investment in a company,
- Capital Surplus – often referred to as paid in capital,
- Retained Earnings – profits earned over time and reinvested in the company,
- Treasury Stock – company stock repurchased by the company (reduces net worth); and
- Contingent Liabilities – represents potential liabilities that may become due and payable if a specified adverse condition occurs at some time in the future (e.g., pending lawsuits, corporate guaranty of another's debt).

5. **Balance Sheet Analysis:**
The balance sheet reflects the assets or economic resources the company owns the debt it owes to creditors in the form of liabilities, and the amount of money the owners have invested in the company in the form of equity. Comparing balance sheets from year to year reflects how well the owners have managed the financial resources of the company.

**General balance sheet information:**
- a. Does it balance? (Do total assets equal total liabilities plus equity?)
- b. Are receivables larger than payables?
- c. If the owner said the cash for the proposed project was coming from cash reserves of the company, is it there?
- d. Are the owner’s reinvesting cash into the company in the form of increases in net worth?
- e. Are intangible assets listed on the balance sheet? You will need to subtract these from equity in order to get a true debt to tangible net worth ratio, since most intangible assets have little value and inflate the equity position of the company's owners.
- f. Is there Officer Debt? Will it need to be subordinated in order to reflect a reasonable debt to equity ratio?
- g. Do the total Receivables and Payables on the Aging of Accounts Receivable and the Aging of Accounts Payable match the respective Receivables and Payables on the interim financial statement?

6. **Balance Sheet Ratios:**
Balance sheet ratios evaluate the ability of the business to generate cash to pay the bills. This is different from the Income Statement ratios where we analyze the ability to control costs. Remember that cash pays the bills, not profits.

**Balance sheet ratios focus on:**
- a. **Liquidity:** Can the company generate cash from current operations to pay the bills?
- b. **Leverage:** How much debt has the company used to finance operations?
- c. **Use of Cash in Operations:**
  - Does the company collect its receivables according to term?
  - Does the company have control over its investment in inventory?
  - Does the company pay its suppliers on time?

**Liquidity Ratios:**
Liquidity ratios evaluate the ability of the company to generate sufficient cash from its current assets to pay its current liabilities. Current assets are the uses of cash involved in the day to day operations. Current liabilities are the sources of cash that pay for the day to day operations of the business.

**Current Ratio:** The Current Ratio provides a ratio of Current Assets or uses of cash to Current Liabilities or sources of cash.
• Current Assets include primarily receivables (sales on terms) and inventory.
• Current Liabilities include payables (supplier debt), accruals (owed to employees) and current bank payments.

The Current Ratio asks this question:
"If the company can collect all of its receivables and turn all of its inventory into a product and sell that product and collect the receivables from that sale, will it generate enough cash to pay its suppliers, employees and its banker?"

\[
\text{Current Assets} \quad \text{Current Liabilities} = \text{Current Ratio}
\]

• A current ratio of 1:1 means that the company has $1.00 in current assets for every $1.00 in current liabilities.
• A current ratio of less than 1:1 means that the company requires additional working capital to cover its cash needs.
• Remember that the current ratio assumes that all receivables can be collected; and, that all inventories can be turned into a sale and collected.
• Look carefully at the RMA ratios for comparison. Some industries, especially those that operate on a cash basis, may typically have current ratios of less than 1:1.

Quick Ratio (Acid Test Ratio): The Quick Ratio eliminates inventory from the analysis. The Quick Ratio is a ratio of Cash (or cash equivalents) and Receivables to Current Liabilities.

The Quick Ratio asks this question:
"If the business had only its cash (or cash equivalent) and was able to collect its receivables, could it make payments to suppliers, employees and the bank?"

\[
\frac{\text{Cash} + \text{Receivables}}{\text{Current Liabilities}} = \text{Quick Ratio}
\]

• In analyzing Quick Ratio, a Quick Ratio of 1:1 means that the company has $1.00 in "quick" assets (cash and receivables) for every $1.00 in current liabilities (supplier, employees, lenders).
• A quick ratio of less than 1:1 means that the company requires additional working capital.
• A company that has a Current Ratio of 1:1 and a Quick Ratio of less than 1:1 has a heavy reliance on inventory as its current assets. The question becomes: "Do they have the ability to convert that inventory into cash?"
• Remember that the Quick Ratio assumes that all receivables can be collected.

Working Capital: Working capital is a measure of the amount of cash after all current assets (cash, receivables, inventory) have been collected and all current liabilities (suppliers, employees, lenders) have been paid.

Working capital asks the following question:
"If the company can collect all of its receivables and turn all of its inventory into a product and sell that product, how much cash is left over after the business pays its suppliers, employees and lenders?"

\[
\text{Current Assets} \quad \text{Current Liabilities} = \text{Working Capital}
\]

• Working Capital is similar to the Current Ratio; the Working Capital Ratio is a short measure of how much working capital a business has to operate the company. To get a better picture of a company’s real working capital, you need to evaluate the operating cycle of the business.
• A positive Working Capital means that the company has excess cash after paying all of the bills. Over time, working capital should be stable or increasing.
• A company with negative working capital should be moving towards positive.
**Debt to Equity Ratio:** The Debt to Equity ratio analyzes how a business has financed its operations. It compares the amount of debt that a company has to its bankers, suppliers, employees and others to the amount of equity that the company has from profits and investment.

**The Debt to Equity ratio asks the following question:**
"How has the company financed its operations between debt and equity?"

\[
\text{Total Liabilities / Net Worth} = \text{Debt/Equity Ratio}
\]

- A Debt to Equity ratio of 2:1 means that the company has $2.00 in debt for every $1.00 in equity. A debt to equity ratio of .40:1 means that the company has 40 cents in debt for every $1.00 in equity.
- The higher the amount of debt, the greater the vulnerability of the company to changes in interest rates, banking climates, and market conditions.
- Over time, the Debt/Equity ratio should be declining. The company should be able to place less reliance on debt and more reliance on reinvested profits.
- A very high debt/equity ratio will severely limit a bank's interest in lending, even in the face of a "good deal."

7. **The Income and Expense Statement:**
The Profit and Loss Statement provides a summary of the revenue generated by a company through the sale of goods or services and a summary of the expenses associated with meeting these sales over a period of time. It is also called an Income and Expense Statement.

<table>
<thead>
<tr>
<th>Income Statement</th>
<th>For the period 00/00/00 thru 00/00/00</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td></td>
</tr>
<tr>
<td>Cost of Goods Sold</td>
<td></td>
</tr>
<tr>
<td><strong>Gross Profit</strong></td>
<td></td>
</tr>
<tr>
<td>Operating Expenses</td>
<td></td>
</tr>
<tr>
<td><strong>Earnings Before Taxes</strong></td>
<td></td>
</tr>
<tr>
<td>Taxes</td>
<td></td>
</tr>
<tr>
<td><strong>Profit (Loss) After Taxes</strong></td>
<td></td>
</tr>
</tbody>
</table>

**Sales:** Net of provision for bad debt, discount and allowances.

**Cost of Goods Sold (COGS) or Cost of Sales (COS):** Expenses directly related to the cost of the product sold for industries, or the Cost of Sales for Commercial firms. It is acceptable accounting practice to allocate certain overhead items, such as rent and depreciation or even officer salary to COGS or COS. When you do your cash flow analysis, remember to add back any depreciation and rents allocated to COGS or COS.

**Gross Profits:** Sales - COGS = Gross Profits.

**Sales, General and Administrative Expenses (SGA):** Net of owner(s) salary, depreciation and amortization, interest and rent.

**Operating Profit:** Gross Profits - SGA = Operating Profit.
**Other Income/Expenses:** Income and expenses not related to sales, such as interest earned.

**Earnings Before Interest and Taxes (EBIT):** Operating Profits - Depreciation - Rent - Interest Owners Salary +/ Other income or expense = Earnings Before Tax.

**Income Taxes:** Federal, state and local taxes on earnings.

**Profit After Taxes:** EBIT - Income Taxes = Profit After Taxes.

8. **Income Statement Analysis:**
The purpose of the financial ratios for the income statement is to measure the ability of the business to control their costs and produce a profit over time. The ratios ask:

- Have the company's sales grown?
- How much of each sales dollar was spent to make the product?
- How much of each sales dollar was left to operate the company?
- How much of each sales dollar was left as profits for the owner?

### Quality Indicator Checklist - Income Statement

<table>
<thead>
<tr>
<th>Income Statement</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are sales increasing?</td>
<td>Yes</td>
</tr>
<tr>
<td>Are Cost of Goods Sold / Cost of Sales as a % stable or declining over time?</td>
<td>Yes</td>
</tr>
<tr>
<td>Industry / Moody's COGS / Sales: _____%</td>
<td></td>
</tr>
<tr>
<td>Are Operating Expenses / Sales as a % stable or consistent over time?</td>
<td>Yes</td>
</tr>
<tr>
<td>Are Operating Expenses / Sales as a % consistent or better than industry?</td>
<td>Yes</td>
</tr>
<tr>
<td>Industry / Moody's SGA / Sales: _____%</td>
<td></td>
</tr>
<tr>
<td>Are profits Increasing?</td>
<td>Yes</td>
</tr>
<tr>
<td>Is the profit margin (EBIT / Sales as a % increasing)?</td>
<td>Yes</td>
</tr>
<tr>
<td>Is the profit margin consistent or better than the industry?</td>
<td>Yes</td>
</tr>
<tr>
<td>Industry EBIT / Sales _____%</td>
<td></td>
</tr>
</tbody>
</table>

**Sales Growth:** Ideally, companies should experience steady growth over time. Special attention should be paid to large increases in sales (fast growth syndrome) which can cause a quick reduction in available working capital.

Sales growth on the income statement can come for a variety of reasons:

- increase in unit prices with no increase in units sold
- actual increase in the number of products sold
- increase in prices forced by an increase in inventory or operations
Compare company performance to trends in the specific industry to determine if the company is consistent with industry.

This Year's Sales - Last Year's Sales / Last Year's Sales = % Sales Growth

Credit Questions Analyzing Sales Growth:
- “What is the long term growth pattern?”
- “Has there been an increase in the actual number of products sold?”
- “What is the history of price increases over time?”
- “Is the sales growth in one particular product or service or is it across the board?”
- “Is the sales growth from one time only increases?”
- “If there have been decreases, why have the decreases occurred?”
- Are the decreases one time due to extraordinary circumstances?
- Does any major growth or decline come from the business of one major customer?

Over time, sales should be increasing evenly. Large sales growth each year indicates a business that is experiencing the "fast growth syndrome". Steady sales decreases should be further investigated.

Cost of Sales: Cost of Goods Sold are the costs to actually manufacture a product. Cost of Goods Sold are variable expenses. As sales increase, Cost of Goods Sold should increase.

On a "percentage of sales" basis, Cost of Goods Sold / Sales should remain stable over time. For example, as the cost of inventory and labor increases, the business should work to be able to raise prices to maintain an adequate profit margin. If the cost of inventory and labor declines, the business can afford to lower prices and still maintain its traditional profit margin.

If Cost of Goods Sold / Sales increases, it means that the business has not been able to pass along cost increases to customers, perhaps due to competition.

Gross Profit: Gross profit is the difference between Sales and Cost of Goods Sold. Gross profits are the funds remaining which must be used to pay the operating costs of the company. Over time, Gross Profit as a percentage of sales should be stable or increasing, indicating that the business has generated profits.

Gross Profit / Sales = Gross Profit & Sales % (Gross Profit Margin)

Over time, the Gross Profit Margin should be stable or increasing. This means that the same or more gross profits from each sale are available to pay the operating costs of the company.

Operating Expenses: Operating expenses ("Sales, General and Administrative" expenses) are those expenses relating to the operation of the company. Operating expenses do not vary with sales since they include such fixed and discretionary expenses as rent, interest, utilities, insurance, office salaries, etc.

Operating expenses as a percentage of sales should be stable or declining over time.

Operating Expenses / Sales = Op. Expense & Sales %

Operating expenses are costs that should not increase as sales increase. They should be stable or declining over time. As such, this ratio should decline as a percent of sales.
**Earnings Before Interest and Taxes:** Is pre tax profit remaining after all expenses of the business. It is used to compensate owners, pay taxes, and to reinvest in the business for growth.

Earnings Before Interest and Taxes/sales should be stable or increasing over time, indicating the ability of the business to increase its profitability.

\[ Earnings \text{ Before Interest and Taxes } / \text{ Sales} = \text{EBIT as } \% \text{ of Sales} \]

9. **The Operating Cycle:**
The operating cycle is a representation of the uses and sources of cash in the operations of a business.

<table>
<thead>
<tr>
<th>Operating Cycle</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Days Receivable</td>
</tr>
<tr>
<td>B</td>
<td>Days Inventory</td>
</tr>
<tr>
<td>C</td>
<td>Days Payables</td>
</tr>
<tr>
<td>D</td>
<td>Days Accruals</td>
</tr>
<tr>
<td>A + B - C - D</td>
<td>Operating Cycle</td>
</tr>
</tbody>
</table>

For example, the business uses cash when it makes a sale on credit, which is called a receivable. It also uses cash to invest in inventory. Also, when a business purchases inventory on credit, it is called a payable. Since employees typically do not get paid daily, the company is purchasing labor on credit as well.

To analyze the operating cycle it is, therefore, necessary to look at the accounts receivables, inventory, accounts payable and accruals in terms of the average number of days it takes to convert these items to cash.

The Operating Cycle is also called the "Cash to Cash" cycle. It focuses on the business' use of cash in Receivables and Inventory and the business' source of cash from Payables.

The Operating Cycle measures how a business uses cash in operations:

The business "invests" cash in receivables (Days Receivable) + The business "invests" cash in inventory (Days Inventory) – i.e., The business "borrows" cash from its suppliers (Days Payable).

**The Operating Cycle asks the question:**
"How long does the business have cash tied up in operations from the first investment in inventory to collecting the sale from the customer?"

**Here are the analysis points to consider:**
- The longer the operating cycle, the greater the need for working capital
- Reducing the operating cycle of a business requires an understanding of which component of the cycle can be reduced
- The Operating Cycle should be stable or declining over time.
- The Operating Cycle should also be consistent or better than industry.

**The formula for Operating Cycle is:**

\[ Days \text{ Receivable} + Days \text{ Inventory} - Days \text{ Payable} = Operating \text{ Cycle} \]
10. **Operating Cycle Analysis:**

**Days Receivable:** The average number of days it takes the company's customers to pay their bills. The day's receivables calculated as follows:

Total Accounts Receivables divided by Total Sales multiplied by the number of days in the statement period. If the statement is for a full year, this figure would be 360. If the statement is six months of operations, this figure would be 180 days.

\[(Receivables + Sales) \times 360 \text{ [days in the statement period]} = \text{Days Receivable}\]

In analyzing Days Receivable, remember the following:

- A Days Receivable of 30 days means that, on average, a business takes 30 days to collect from its customers
- Days Receivable should be:
  - Consistent with terms offered to customers
  - Consistent or better than the industry
  - Stable or declining over time

**Days Inventory:** The average number of day's worth of the inventory on hand, or how long cash is tied up in the production cycle before it is sold.

The Days Inventory is calculated by dividing inventory by cost of goods sold and multiplying by the number of days in the statement period.

\[(\text{Inventory} / \text{Cost of Goods Sold or Cost of Sales}) \times 360 \text{ [days in the statement period]} = \text{Days Inventory}\]

In analyzing day's inventory, consider:

- The longer the days inventory, the more cash that the business has tied up in production which is not available to pay bills
- This is particularly important for manufacturing businesses who must always focus on reducing their manufacturing time and how much they must warehouse.
- Day's inventory should be generally consistent with the production cycle.
- Over time, Days inventory should be stable or declining.

Day's inventory should be consistent or better than the industry.

**Days Payable:** The average number of days it takes the company to pay its trade suppliers. The ability to pay suppliers is determined by the ability of the business to generate cash from its receivables and to "turn" its inventory. Day's payable is calculated by dividing Accounts Payables by COGS or COS multiplied by the number of days in the statement period.

\[(\text{Payables} / \text{COGS or COS}) \times 360 \text{ [days in the statement period]} = \text{Days Payable}\]

**Days Payable should be:**

- Consistent with the terms offered by suppliers
- Consistent or better than the industry
- Stable or declining over time
**Days Accrual:** The average number of days it took the company to pay accrued expenses (wages, benefits, payroll taxes, etc.). Day’s accrual is calculated by dividing accruals by COGS or COS and multiplying by the number of days in the statement period.

\[(\text{Accruals} / \text{COGS or COS}) \times 360 \{\text{days in the statement period}\} = \text{Days Accruals}\]

The Operating Cycle is:

\[
\begin{align*}
&+ \text{ Days Receivable} \\
&+ \text{ Days Inventory} \\
&- \text{ Days Payables} \\
&- \text{ Days Accruals} \\
&= \text{ Operating Cycle}
\end{align*}
\]

A shorter Operating Cycle means that a company has a lesser need for working capital. A longer Operative Cycle means that a company has a greater need for working capital.

Moody’s will record day’s receivable, inventory and payables, but not accruals. To provide a comparison between the business and industry, it will be necessary to eliminate day’s accruals from this calculation.

11. **Reconciliation of Net Worth:**

The reconciliation of net worth compares the net worth among two years to measure the amount of new equity (or withdrawals) of equity between two years.

\[\text{This Year's Net Worth} - \text{This Year's Profit} - \text{Last Year's Net Worth} = \text{New Equity (Withdrawal)}\]

At the end of the year, the business adds its current profit to its Net Worth if it reinvests the profit in the operations of the business. If the profits are not reinvested, the amount is taken out of Net Worth.

In Sub S corporations, cash may be taken out of the company for the purpose of paying taxes or for owner’s compensation. A Sub S corporation may show all profits being taken out of the business.

The reconciliation of net worth asks the questions:
"Over the past year, has the business owner added or taken out any equity from the company?"

- The Net Worth is taken from the balance sheets; the profit is taken from the Income Statement
- If the business owner has put new equity into the company, what is the source of the new equity?
- Has the business put any new officers’ debt into the company instead of equity? Is the officer’s debt subordinated?
- If the owner has taken cash out of the company, what was the cash used for?
- If the business is a Sub S corporation, was the cash really taken out?

**Re: Personal financial statements:**

In order to measure the financial strength of an individual guarantor outside of the Borrowing entity’s interest, the individual’s net worth should be adjusted by deducting the overstated portion of an asset’s value and the understated portion of a liability’s value. Conversely, and in the rarer situation where an asset may be undervalued or a liability overstated, it may be appropriate to increase the understated asset or decrease the overstated liability. Common adjustments to the book net worth of an individual are as follows:
Net Worth:

Less: Decline in value of stocks and bonds
Less: Decline in investment in borrower’s firm
Less: Amounts due from related parties
Less: Ownership interests less than 50%
Less: Net equity in personal residence
Less: Personal assets (i.e. Furniture, jewelry, etc.)
Less: Any other assets of unsubstantiated value.
Less: Estimated personal income taxes payable
Less: Any other liabilities not already disclosed
Plus: Appreciated value of stocks, bonds, and real estate
Plus: Overstated portion of any liabilities

12. Capital Expenditures:
The Capital Expenditures analysis determines whether the company had acquired new fixed assets, or whether it has sold fixed assets. Included would be any form of fixed assets: land, building, equipment, leasehold improvements, etc. Many businesses, particularly those in manufacturing, have ongoing needs to repair and replace equipment and expand their buildings.

The Capital Expenditures Analysis asks the question:

"How much has the business invested in new equipment and real estate over the past year? Has the business sold any real estate or equipment over the post year?"

This Year's Net Fixed Assets (NFA) - This Year's Depreciation - Last Year's NFA Capital Expenditure (Sale of Assets)

Businesses that must spend funds each year for capital improvements need to factor in the costs of financing and the need for cash.

Evaluate how capital Investment is financed:

- How much debt at what rate and term?
- How much equity?
- What is the purpose of the investment?
- How will it help the business?

13. The Financial Projections:
The historical financial statements reflect how well management has deployed the company's resources, and are a picture of the company's financial health. Projected financial statements force management to think through the impact of this investment in fixed assets on the balance sheet of the company. It also forces them to think through the impact of additional costs related to occupying larger space on the operations of the company if the company is expanding into larger facilities with the project.

Most loan requests will not rely upon projected sales and profits to service debt on the contemplated project. If this is the case, this is a high risk loan. Perhaps the company is really not in a position to be investing in this size project at this time. Or, perhaps there are options you might want to consider in mitigating the risk
in this project. However, with a start up business, you will only have projections to work with. Ask yourself:

a. Are the projections logical and reasonable? Are they consistent with historical numbers and ratios?
b. Do sales appear to be attainable?
c. Has management accounted for increases in occupancy costs? Increases in wages sufficient to support job creation projections?
d. Ask for explanations for major differences from historical numbers, such as large sales increases, changes in operating cycle ratios and reduction in operating costs.
e. Review the assumptions for financing to assure they are accurate and current.
f. Projections can be used to complete "what if" analyses to determine what happens if changes take place in operations.
g. Accurate and realistic projections can be helpful in determining a business' need for working capital in the future.
h. Remember: Projections typically show that the business can repay the debt!

With start up businesses, the owners will be required to provide a month by month operating cash flow projection along with written assumptions so you understand how they arrived at the numbers they used in the projections. Study these carefully and ask questions if they don't make sense or if you question how attainable they might be.

Pay particular attention to the pre opening expenses the owners typically will invest in order to open their doors for business. These expenses will occur at least 30 days and sometime as early as 90 days prior to any income the company will receive.

Look for seasonality in the business. You may need to research this industry a bit if you're unfamiliar with it.

There are additional cash injection requirements for a start up business. And, you'll want to require additional cash for working capital to take them through the start up stage to profitability. You may also consider additional reporting requirements for the start up years until you are comfortable the company has reached a level of operational stability and is no longer considered a high-risk loan. This is a business that you want to place under frequent watch once it is closed.

B. Cash Flow Analysis

Cash Flow Analysis is determining the ability of a business to repay debt is done by analyzing the income statement and completing a Cash Flow Analysis. Cash Flow Analysis involves comparing:

- Cash available for debt payment, and
- Required debt service for the financing

<table>
<thead>
<tr>
<th>Cash Flow Analysis</th>
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</thead>
<tbody>
<tr>
<td>(A)</td>
</tr>
<tr>
<td>(B)</td>
</tr>
<tr>
<td>(A / B)</td>
</tr>
<tr>
<td>(A - B)</td>
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</tbody>
</table>
Comparison of total cash flow with debt service on all loans is called Cash Flow Coverage Ratio.

\[
\text{Cash Flow / Debt Service} = \text{Cash Flow Coverage Ratio}
\]

where:

\[
\text{Cash Flow} = \text{Earnings Before Tax (EBIT) + Depreciation + Amortization Expense + Interest Expense + Rent Savings (or other savings)}
\]

and

\[
\text{Debt Service} = \text{Principal and interest on project debt + Continuing annual principal and interest payments on debt}
\]

Thus:

\[
\text{Excess Cash Flow} = \text{Cash Flow - Debt Service}
\]

Continuing annual principal and interest payments on debt can come from the Schedule of Debt Obligations or from current portion long-term debt (Balance Sheet) plus interest expense on the Income Statement.

| Cash Flow Analysis |
|-------------------|----------------|
| Information Source | 19___ | 19___ | 19___ |
| Earning Before Tax  | P&L   | $     | $     |
| + Depreciation      | P&L   |       |       |
| + Interest          | P&L   |       |       |
| + Interest          | P&L   |       |       |
| + Saved Rent        | P&L   |       |       |
| + Other Savings     | P&L   |       |       |
| - Officers Withdrawl| NW Reconciliation |       |       |
| Total Cash Flow (CF)|       |       |       |
| + Project Debt Service (P&I)| Borrower Request |       |       |
| + Existing Debt Annual P&I| Schedule of Debt |       |       |
| + Other New Debt Service| Schedule of Debt |       |       |
| + Other New Costs   | Borrower Request |       |       |
| Total Debt Service (DS)|       |       |       |
| Cash Margin / Cash Flow Coverage|       |       |       |
| Cash Flow Coverage Ratio|       | :1   | :1   | :1   |
1. **Analyzing Cash Flow Coverage:**

   A Cash Flow Coverage Ratio or debt coverage ratio of 1.10:1 means that the business has $1.10 for every $1.00 in debt service.

   The goal for minimum debt coverage is 1.25 meaning $1.25 in cash flow for every $1.00 in debt service. Search for additional cash flow if the business has a Cash Flow Coverage Ratio of less than 1:1.

   **Critical Questions to ask:**
   a. Can the business make the monthly debt service payments on all debt?
   b. Are there any secondary (non project) sources of cash flow available to make payments?
   c. Does the business have enough working capital to finance its growth while expanding?
   d. Will the company experience additional savings/expenses from the new project?
   e. Rent Savings?
   f. Reduced expenses (labor, material, etc.)?
   g. Increased expenses (utilities, property taxes, interest?)
   h. Can/will the company reduce discretionary expenses if needed?

2. **Determining Debt Capacity:**

   Before you structure specific financing, it is possible to determine the ability of a company to support financing. This can be helpful to a business when they are first considering expanding and want to analyze how much debt they can afford before they begin the process.

   The ability of a company to support financing will be based upon:
   - Cash flow of the business, and
   - Terms and conditions of proposed financing

   **Step 1:**
   How much cash flow (CF) is available for debt service (DS)?
   \[
   \text{Profit after Tax} + \text{Depreciation} - \text{CLTD} = \text{CF for D/S}
   \]

   **Step 2:**
   Debt Coverage Ratio: What is the bank's DCR cash flow coverage ratio (DCR)?

   **Step 3:**
   Adjusted Cash Flow: What is the adjust CF for DS?
   \[
   \text{CF for DS} + \text{Bank DCR} = \text{Adjusted CF for DS}
   \]

   **Step 4:**
   What are the terms and conditions on proposed financing?
   - Rate
   - Term
   - Constant
Step 5: Debt Capacity: How much debt with the Adjusted Cash Flow support?

\[
\text{Debt Capacity} = \frac{\text{Adjusted CF}}{\text{Constant}}
\]

3. Abbreviations and Definitions:

- **Adj. CF**: Adjusted Cash Flow: The amount of cash flow available for debt service after factoring the lenders desired debt coverage ratio (DCR).
- **CF**: Cash Flow: The amount of cash available in a business to make debt service payments.
- **CLTD**: Current Portion of Long-term Debt. The principal payments on term loans due in the next 12 months.
- **DCR**: Debt Coverage Ratio: The amount of "cushion" a lender wants for loan payments. A DCR of 1.5 means that the lender wants $1.50 in Cash Flow for every $1.00 in Debt Service.
- **Debt Capacity**: The amount of debt that a business can afford based upon the Adjusted Cash Flow.
- **DS**: Debt Service: The annual principal and interest payments on a loan.

4. Determining Debt Capacity – An Example:

**Example:**

**Step 1:** How much cash flow (CF) is available for debt service (DS)?

\[
\text{Profit after Tax} + \text{Depreciation} + \text{CLTD} = \text{CF for D/S}
\]

\[
\begin{align*}
\text{Profit after Tax} & = $100,000 \\
+ \text{Depreciation} & = 25,000 \\
- \text{CLTD} & = 10,000 \\
\hline
\text{CF for D/S} & = $115,000
\end{align*}
\]

**Step 2:** Debt Coverage Ratio: What is the bank's cash flow coverage ratio (DCR)?

\[
\text{DS} \times \text{DCR} = \text{Adjusted CF for DS}
\]

\[
\begin{align*}
\text{DS} & = \text{Bank DCR} \\
& \approx 1.5 \\
\text{Adjusted CF for DS} & = $76,660
\end{align*}
\]

**Step 3:** Adjusted Cash Flow: What is the adjust CF for DS?

**Step 4:** What are the terms and conditions on proposed financing?

**Step 5:** Debt Capacity: How much debt with the Adjusted Cash Flow support?

**Example:**

**Step 1:** How much cash flow (CF) is available for debt service (DS)?

\[
\begin{align*}
\text{Profit after Tax} & = $100,000 \\
+ \text{Depreciation} & = 25,000 \\
- \text{CLTD} & = 10,000 \\
\hline
\text{CF for D/S} & = $115,000
\end{align*}
\]
Step 2: Debt Coverage Ratio: What is the bank's cash flow coverage ratio (DCR)?

\[ \text{DCR} = 1.50 \]

Step 3: Adjusted Cash Flow: What is the adjusted CF for DS?

\[
\text{CF for DS} = 115,000 \\
+ \frac{\text{Bank DCR}}{1.50} \\
= \text{Adjusted CF for DS} = 76,660
\]

Step 4: What are the terms and conditions on proposed financing?

Rate 9.00%
Term 10 Years
Constant .1520

Step 5: Debt Capacity: How much debt with the Adjusted Cash Flow support?

Adjusted CF $76,660
Constant .1520
Debt Capacity $504,386

5. Personal Financial Information:

Personal financial statements must be current within 90 days.

- **Who must provide personal financial statements?**
  
  Anyone who owns 20% or more of the business.

  There may be a situation where there is an additional guarantee from a third party who is guaranteeing the loan. If this person is not a 20% or more owner of the business their personal financial statement is needed to support the guarantee. The guarantee is in place because this person is adding a financial comfort to the credit. Therefore, it is important to have their personal financial statement.

- **Evaluating Personal Financial Statements**
  
  Personal financial statements are evaluated for the following:

  a. Determine the value of a personal guarantee for any financing
  b. Verify the availability of cash equity for the project
  c. Verify information on the business financial statements
  d. Determine the ability of the owner to provide additional equity if needed or to forgo officers compensation if needed to justify cash flow
  e. From the standpoint of financing, the information that is critical to the evaluation is:
    
    - Who owns the business?
    - How is the business valued on the Personal Financial Statement?
    - Are there any assets that are owned by the individual and leased to the business? If so, is there any debt financing on those assets?
    - What is the level of owner’s compensation?
    - If an owner is highly compensated, does the compensation "flow through" to personally owned assets or investments?
    - Are there any personal obligations which would prevent the owner from focusing on the business?
- Does the Personal Financial Statement show any assets which could be used as secondary collateral in the event that additional collateral was requested?
- Does the Personal Financial Statement reflect assets owned jointly or separately?

**When would a personal cash flow be advisable?**

A personal financial statement is not a statement of personal cash flow. A personal cash flow identifies the amount and sources of income of an individual, and the personal expenses of an individual.

You'll notice that an increasing number of bank financial statements now include a personal cash flow as a section on their form.

There will be times that analyzing the company's cash available for debt service on the loan shows insufficient cash flow to service the debt. One option that may be available would be a limitation on officer's salary. This is only an option if the officer(s) can afford the decrease in officer's salary. The personal cash flow will provide you with information that will indicate whether this is a viable option. You may want to verify certain information on the personal cash flow form or evaluate the expense side to determine if logic tells you this is an option that makes sense.

6. **Cash Flow Verification:**

To ensure the reliability of the underwritten Net Cash Flow (NCF), the Local Originator/Underwriter must take steps to confirm the accuracy and reasonableness of all data submitted by the Borrower. These steps will generally include a review and comparison of a variety of Borrower provided data for consistency, as well as comparing this data with relevant published industry data and/or market information provided in the appraisal or obtained independently by the Local Originator/Underwriter. Finally, for certain property types, such as transactions where there has been a higher degree of volatility in historical income and expenses, or properties where a significant amount of collections are received in cash, the CEF Pilot may require Agreed Upon Procedures.

The verification of historical and projected property income entails both a detailed analysis of leases (including all amendments, modifications, and extension agreements) and a review of other data that can support or verify information reported in the property operating statements. The verification process should include, at a minimum, the following steps:

- Abstract leases and compare to rent roll,
- Compare estoppels to rent roll and lease abstracts,
- Compare operating statements to tax returns,
- Compare deposits from last three months bank statements to monthly operating statements to support collection history,
- Compare projected reimbursement income and operating statement expenses to tenant CAM billing statements,
- Compare historical percentage rent collections to tenant sales reports,
- Compare tax, insurance, and utility bills to historical statements,
- Compare management and other service contracts to operating statements,
- Review capital expense schedule; obtain receipts for larger capital expense items; confirm capital improvements through property inspection and/or engineer’s property condition survey,
• Compare historical and underwritten TI/LC expenses to leases signed in the last three years; and
• Compare historical operating expenses to appraisal estimates, comparable properties, and industry standards such as the American Institute of Real Estate Appraisers, Data Resources Inc. (McGraw-Hill), and Construction Cost Data (Marshall Swift).

Any significant discrepancies uncovered through these procedures must be identified and resolved prior to funding. Receipts, correspondence or other data provided to support or reconcile cash flow information must be included in the Underwriting Binder and referenced in the MLA.

C. Repayment

1. Ability to Repay (Capacity):
   A major component of the financial underwriting of the loan is the review and analysis of a business’ cash flow. A determination will be made if the business borrower has the capacity to repay the loan from its operating cash flows. Ability to repay can be defined as the capacity of the borrower to have cash available for new and existing debt service payments and is usually measured as net operating income divided by debt service. This simple calculation, commonly known as Debt Coverage Ratio (DCR), indicates the magnitude of the cushion that a prospective project has in paying debt service. All businesses, to whom credit is extended, must provide evidence of a primary and secondary repayment source.

   Borrows must demonstrate financial capacity to:
   a. Meet proposed repayment terms
   b. Fulfill other financial obligations, and
   c. Maintain a safety cushion in the event of unforeseen setbacks.

   Repayment capacity and capital must be considered in light of the general economic, competitive, and other conditions to which the borrower is exposed. Projects that increase the debt service coverage ratio by using balloon financing will be carefully reviewed. The debt service coverage ratio is estimated using the interest rate the borrower is obligated to pay in its debt to the fiscal agent.

2. Collateral:
   When debt is not repaid as scheduled from business cash flow, collateral must be used as a secondary method of repayment. Collateral for a loan comprises any assets pledged to guarantee repayment of the loan. Loans must have collateral sufficient to ensure loan repayment from the pledged assets in the event that the business defaults on its loan payments, because it cannot generate cash flow sufficient to service the debt. Collateral must be liquidated (by selling it) in order to obtain the cash to repay the outstanding loan balance. The costs of liquidation, time delays, and the fact that the highest price is rarely obtained in a distress sale, will reduce the cash obtained in liquidation to effectively pay off the loan principal.

   In order to compensate for the reduced proceeds which may arise from unforeseen liquidation of collateral, varying discount rates will be used to estimate the value of the collateral being pledged, against the loan at the time of origination. The discount used to value the collateral is based on the anticipated ease of liquidation, and the likelihood that the asset will maintain its value in the market.

   A determination must be made whether the asset being financed is a specialized asset. Specialized assets have a limited market for resale due to unusual design features, amenities or characteristics which restrict general use. The loan to value may be reduced to compensate for greater collateral risk. The minimum loan to value ratio is 80% for a Section 108 Loan. Examples of specialized assets are: nursing homes, recreational facilities, etc.
For economic development loans, pledged collateral may include: working capital, machinery and equipment, real estate or other resources and assets.

NOTE: A Section 108 Loan will not take less than a second lien position on real estate or other collateral.

3. **Working Capital:**
   Working capital is defined as the excess of current assets over current liabilities. This simple accounting definition belies the importance of working capital and the process by which cash is invested in current assets, converted to cash, and used to pay current liabilities in an operating company. Working capital is not cash. The quality of working capital is the prime determinant of cash flow.

4. **Machinery & Equipment:**
   Machinery and equipment are fixed assets that a company could pledge as collateral for a loan. When assessing the value of this collateral, examine the types of machinery and equipment that are being pledged to determine its value. In general, loans secured by machinery and equipment will have a loan value of 50 to 75 percent.

5. **Real Estate:**
   A business may choose to pledge real estate as collateral for loans. For real property that is to be offered as collateral, carefully review the appraisal (if possible no more than 90 days old) of the real property in order to determine the value of the subject property. Also, access and review a current title report of the subject property (if possible, no more than 30 days old) in order to determine the existing encumbrances or easement rights which affect the property. Note, title companies or lawyers usually charge a fee to obtain a title report.

6. **Guarantees:**
   Third party guarantees of loan repayment are issued by individuals and corporations related to the company. They are used when the borrower is unable to meet loan commitments from cash or collateral. Third party guarantees from the company’s principals and from parent corporations are advisable, even if they appear to have little worth.
# Proposed Sources & Uses of Funds Form
## PA Section 108 Loan Guarantee Program

**Public Entity:**

**Project Name:**

**Project Location:**

<table>
<thead>
<tr>
<th>Use of Funds</th>
<th>All Sources of Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Activity / Line Item</td>
<td>Section 108 Funds</td>
</tr>
<tr>
<td><strong>Subtotals:</strong></td>
<td></td>
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</tbody>
</table>

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Appendix A
# Proposed Job Category Form

## PA Section 108 Loan Guarantee Program

<table>
<thead>
<tr>
<th>Public Entity:</th>
<th>Project Name:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Project Location:</td>
<td>Firm's Name:</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Job Category/Title or Classification</th>
<th># of Jobs to be Created</th>
<th>Yearly Salary</th>
<th>Hourly Wage</th>
<th># of Full Time Jobs</th>
<th># of Part Time Jobs</th>
<th>Benefits Provided</th>
<th>Comments</th>
</tr>
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<tbody>
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<td><strong>Subtotals</strong></td>
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</table>
Proposed Project Underwriting Form
PA Section 108 Loan Guarantee Program

Public Entity: __________________________________________
Project Name: __________________________________________
Project Location: ________________________________________

1. Type/category of project:
   - ☐ Housing
   - ☐ Community Development
   - ☐ Economic Development

2. State CDBG Status:
   - ☐ Entitlement jurisdiction
   - ☐ Non-entitlement jurisdiction

3. Project costs are reasonable:
   - ☐ Sources & Uses Form submitted
   - ☐ Price quotations submitted
   - ☐ Architect/engineer’s estimates provided
   - ☐ Appraisals provided
   - ☐ Sales agreements submitted
   - ☐ Other

4. All sources of project financing are committed:
   - ☐ Letters if intent/commitment for loans
   - ☐ Copies of loan applications submitted
   - ☐ Grant commitment letters submitted
   - ☐ Cash equity is available
   - ☐ Third party financing is secured

5. Sec. 108 Loans are not substituted for non-federal funds.
   - ☐ A project financing gap is identified
   - ☐ Financing gap is documented

6. Project is financially feasible:
   - ☐ Balance sheet is submitted
   - ☐ Principal’s statements are submitted
   - ☐ Income and expense costs are reasonable
   - ☐ Costs compare to industry averages.
   - ☐ Past, current & future financial data submitted
   - ☐ Job estimates are reasonable
   - ☐ Labor costs are within industry averages
   - ☐ Interest rate and loan term are appropriate

7. Return on equity investment:
   - ☐ Amount of owner cash into project is supported.
   - ☐ Projected revenues are documented
   - ☐ Owner’s salaries & expenses are reasonable
   - ☐ Owner’s draws are documented
   - ☐ Debt service is supported
   - ☐ Net operating income is reasonable
   - ☐ Owners are not being unduly enriched
Proposed Project Review Checklist
PA Section 108 Loan Guarantee Program

Public Entity: _____________________________________________
Project Name: ___________________________________________
Project Location: __________________________________________

☐ Applicant is a member of PA Section 108 Loan Consortium.
☐ Category or type of project is identified.
☐ Project meets the Section 108 eligibility criteria.
☐ Regulation citation is identified.
☐ Project meets a National Objective.
☐ Public benefit will be achieved.
☐ Job creation or retention has been documented.
☐ Underwriting analysis is completed.
☐ All sources & uses of funds have been identified.
☐ Project feasibility is supported by third party documentation.
☐ Project site and location are suitable.
☐ The development team is identified and has the capability to do the project.
☐ Sources of loan repayment have been identified.
☐ Additional loan security or collateral has been identified.
☐ The citizen participation process has been followed.
☐ Resolution by local governing body has been passed.
☐ Section 108 loan certification forms have been signed.