



LOAN SERVICING

What do we do after the loan is made?



Loan Servicing

“Just as important as loan underwriting!”

- **Documented Communication**
 - Texts
 - Lender Liability
- **Ongoing Borrower Solvency & Viability**
 - Red Flags
 - Early Warning Signs
- **Collateral (Secondary Repayment Sources)**
 - Lien Perfection
 - Condition & Value Monitoring
- **Loan Conditions & Covenants**
 - Formal means of tracking both

Loan Servicing

“Just as important as loan underwriting!”

- **Can Vary by Loan Type**
 - **Term Loans**
 - Collateral Types (RE vs M&E vs Livestock, etc)
 - Pay as agreed
 - **Construction Loans**
 - Projected Costs vs Actual Costs
 - Lien Waivers
 - Permanent Financing in place
 - **LOCs**
 - Expected Peak vs Actual Peak
 - Cap Ex
 - Liquid Collateral

Loan Servicing

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- **Documented Communication**

- File organization
 - Consistent defined structure
 - Credit Review, Audit, Regulator
 - File Comments
- Correspondence
 - Written Letter
 - Email
 - Text
 - Fax
 - Voicemail



Loan Servicing

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- **Ongoing Borrower Solvency & Viability**

- Use of Funds
- Credit Bureau Reports, Dun & Bradstreet, background checks
- Financial reporting and documentation
- Communication going dark
- Rising accounts payable



Loan Servicing

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- **Collateral (Secondary Repayment Sources)**

- **Lien Perfection (First to file)**

- UCCs (Chattel property)
 - Blanket
 - PMSI
 - Specific (Cattle, Piece of Equipment, Crop or Crop type, etc.)
 - Caretaker filings
 - Pre-closing & Post-closing UCC lien searches
 - Subordinations
- **Mortgages (CREMs vs REMs)**
 - Title policy/Title opinion/Title search
 - Paid RE Taxes
 - Flood verifications



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- **Collateral (Secondary Repayment Sources)**

- **Lien Perfection (First to file)**

- **Continuations**
 - Tickler System
- **Assignments**
- **Superior Liens (lien waivers?)**
 - Mechanics
 - Agister's
 - Feed?
- **Lien Waivers**
 - Landlord waivers

Assignments of

- **Rent**
- **Contracts (Ex. Swine & Poultry)**
- **Program payments-CRP, etc**
- **Life insurance-cash value or proceeds**
- **Crop insurance**
- **Commodity or hedge account**
- **Livestock feeding or care agreements**

Loan Servicing

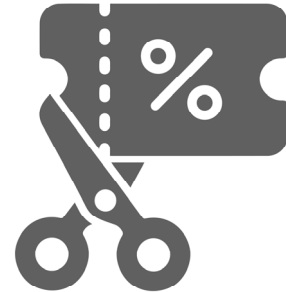
“Just as important as loan underwriting!”

- **Collateral - Secondary Repayment Sources**
 - **Condition & Value Monitoring**
 - Inspections vs farm visits
 - Third Party inspections
 - Evaluations
 - Certified Appraisals
 - Insurance
 - Environmental compliance
 - Livestock brand areas



Valuing Collateral

- **Start with Market Value**
- **Apply Discounts per bank policy**
 - Going concern vs. Liquidated values
 - Market volatility
 - Expense to get to market
 - Prior liens
 - Accounts Payables



Inspection Process?

- **Obtain true & correct information**
- **View, Compare & Analyze**
 - Checkbook review
 - Reconciliations
- **Signatures**

★ Accuracy is King

★ Trust but Verify



Appraisal Issues

- Appraise or Not
- Engagement
- Real estate vs. Chattel (frequency)
- Appraisal Review
- Declining Value environment



Insurance

- Assignment
- Loss Payee & Mortgagee
- Proof
 - Types
 - Crop
 - Livestock
 - P & C
 - Life
 - Health
 - Disability
 - LTC



Environmental Compliance

- Environment Surveys
- Permitting
- Farm Program Compliance
- Visual Inspection
- Hazardous Waste?



Loan Servicing

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- Loan Conditions & Covenants



How can conditions and covenants make a difference?

- They set the fence
- Get customers attention
- Prompt (force) customer action
- Reduce credit risk and rate
- Assist with collection
- Maximize recovery

Conditions

- Loan amount**
- Terms**
(Amm, Pymt Frequency, Rate, Collateral, etc.)
- Controls & monitoring devices**
- Loan Agreements**
- Borrowing Base Reports**
(defined in the Loan Agreement)
- Equity Margin Agreements**
- Additional Security**
- Guarantees**
- Balloon Payments**
- Assignments**
- Contracts**
- Entity docs** (Operating Agreements)
- Financial reporting**
- Reporting frequency**
- Compliance Certificates**
- MOUs**

Guarantees

- **Secured or Unsecured**
- **Limited or unlimited**
- **Individual**
 - Spousal consent
 - Communication
- **Corporate**
- **Government (FSA, B&I, SBA, etc)**



Covenants

- **Loan Agreements**
 - **Affirmative covenant examples (Will do)**
 - Maintain financial ratios
 - Working Capital level (Borrowing Base Report)
 - Owner Equity level
 - Reporting frequency
 - **Negative covenants examples (Won't do)**
 - Cap Ex restrictions
 - Incur New Debts
- **Compliance Certificate**
 - Borrower going on record stating compliance or non-compliance with each covenant

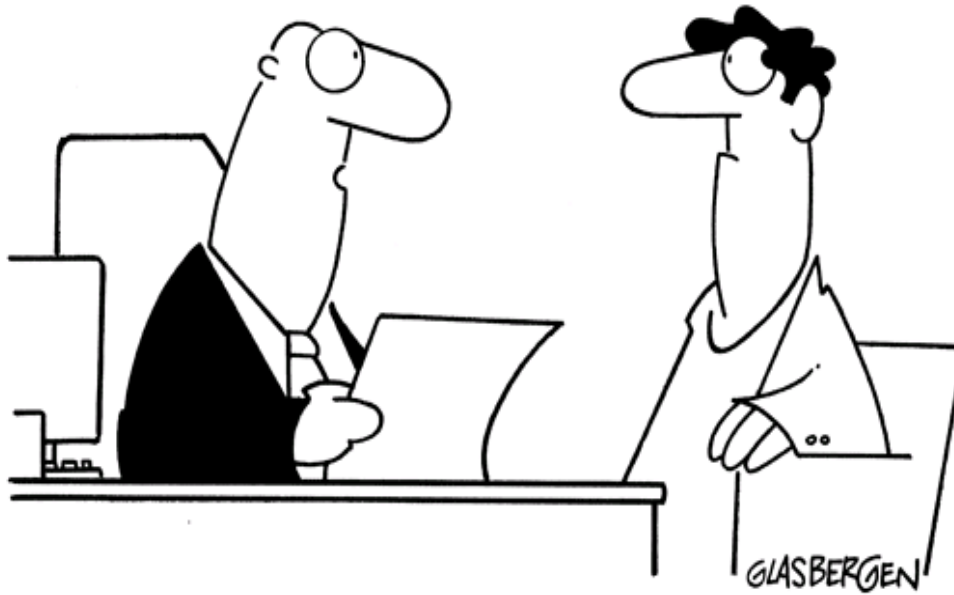
Loan Agreements

- **Manage it or don't do it!**
- **If covenants are tripped, deal with it!**
 - Waiver
 - Reservation of rights
 - Legal action



RISK MANAGEMENT





**“Banks are being more cautious these days.
For mortgages, we require 300% down-payment to
cover whatever crisis may show up in tomorrow’s news.”**



How Do We Manage Risk?

Identify who in your portfolio is most vulnerable.....

And why!



How Do We Manage Risk?

- **Risk Rating systems**

- More than one way works

- **Example:**

- 1-Excellent; 2-Good; 3-Pass; 4-Marginally Satisfactory; 5-Pass Watch; 6-Special Mention; 7-Substandard; 8-Doubtful; 9-Loss

- **Objective: Financial measurements**

- **Subjective: Management**

- (6th C)
- Don't weight too heavily
 - Production
 - Financial
 - Leadership (Execution)

Signs of Distress/Problem Credits

- **Early Warning Signs**

- Tax returns look strong, but BS earnings are deteriorating.
- Deterioration of Collateral Margin.
- Notable increase in consumer debt.
- Late pays/collections on the CBR.
- Frequent overdrawing of the DDA's.
- Grain reconciliation.
- LOC that is evergreen
- Change in communication (Go dark)
- Changing vendors/accountant
- Others????



Signs of Distress/Problem Credits

- **Late Warning Signs**

- Falsified financials (fraud)
- Grain reconciliation (fraud or inadequate record keeping systems)
- Livestock inventory discrepancies
 - Claiming others livestock as theirs
 - The float game
 - Conflicting Claimants



The Dreaded Three D's

- **Disability**
- **Divorce**
- **Death**



Worst Management Practices of Agricultural Bankers

- Five “C’s” of lending called collateral, collateral...
- Too busy and understaffed
- Timeliness
- Not understanding communications style
- Credit scoring without verification
- Providing advice not alternatives (options)
- Surprise lending
- Loan file documentation not in writing
- Too many covenants not enforced
- Other

RULES TO LIVE BY



Rule #1:

You are a lender, not a speculator

Don't throw good money after bad



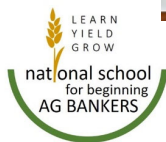
Your first loss is your least loss



Rule #2:

Require a financial roadmap

“Don't tell me what you value, show me your budget, and I'll tell you what you value.”



Rule #3:

If it doesn't feel right, don't do it



Rule #4: **Don't go at it alone**



Sunlight is the best disinfectant
Losses go with the territory
Zero losses means zero loan growth.

Sam's Control Story