SBLF - A DEEPER DIVE INTO THE DETAILS

by Steve Brown

Last week we updated our readers on the Small Business Lending Fund or "SBLF" (See Feb 1 Banc Investment Daily) and delved into some of its major components. Today, we take a deeper dive to get into some of the more nuanced details that our own research team

uncovered while conducting an in-depth analysis on this capital enhancing opportunity.

SBLF is intended to increase loan availability for small businesses, so rules are written around that premise. For instance, 90% of any capital contributed by the Treasury must be pushed down to the bank subsidiary from the holding company level. The expectation is that once banks have the capital, they will seek ways to lend it out in order to improve performance.

Banks that participate will have to certify adherence to anti- money laundering requirements (in particular the customer identification program), before receiving the investment and submit an annual certification from their auditors (that the processes and controls used to generate the reports are accurate) regarding their reports (as well as their adherence to borrower standards). Quarterly, banks will have to submit dividend rate calculations and lending information. In addition, banks and bank holding companies must annually certify that the principals of the businesses that receive qualified small business funding have neither been convicted of nor pled nolo contendre to a sex offense against a minor. Quarterly Call Reports require supplements to identify additional small business lending for any bank that borrows through SBLF.

While no portion of lending guaranteed by the Government or a 3rd party will be considered a qualified small business loan (i.e. SBA loans), the unguaranteed portion can qualify. Put another way, the guaranteed portion is subtracted from the loan amount, as is any portion assumed by another party (i.e. participations).

Banks are eligible to apply to receive funds under SBLF, as long as they were less than $10B in asset size as of Dec 31, 2009. Banks can apply to participate until Mar 31, 2011. To participate, banks must submit an application form (www.treasury.gov/SBLF) and a small business lending plan of approximately 2 pages (to your primary regulator and state regulator if applicable). The plan must address how the bank will use the funds to increase small business lending in its community; how much lending the bank expects to do as a result of the receipt of funds and proposed outreach and advertising efforts to inform members of the community about how to apply for small business loans.

Another consideration is that while Basel III seems to indicate SBLF shares could be subject to full capital de-recognition (as Tier I) as early as January 1, 2013 (or as late as 2015); we expect regulators to address this (and prevent that problem from occurring) as part of the final Basel implementation in the US.

Banks that are rated a CAMELS 4 or 5 are not eligible, nor are banks that have been upgraded in the previous 90 days. Further, banks that receive capital under SBLF can also repay it at any time, with permission of their primary regulator. Partial payments are also allowed, provided they are at least 25% of the original funding amount. Banks can also still continue existing dividend and share repurchase practices, uninterrupted.

Banks must originate loans to customers in sizes of less than $10mm, so it is important to note that a group of loans to the same borrower or any of its affiliates will be treated as a single loan by the Treasury. Net charge-offs are added back to the small business originated total, so as not to penalize banks for appropriately charging off loans.

There is absolutely no downside to applying, since doing so does not create an obligation. If you are approved by Treasury for the investment, you will then have a reasonable amount of time to turn it down. We say fill out the paperwork, get approved and continue to dive deeper into your due diligence process, to determine whether or not this capital is right for you.

BANK NEWS

Bank Closures (14 YTD)

Regulators closed 3 banks on Fri: 1) American Trust Bank ($238mm, GA) was sold to Renasant Bank ($4.2B, MS). Renasant took all deposits (no premium) and $147mm in assets (64% under loss share). 2) North Georgia Bank ($153mm, GA) was sold to BankSouth ($250mm, GA). BankSouth purchased all non-brokered deposits and $124mm in assets. The FDIC will pay brokers directly to repay the CDs. 3) Community First Bank - Chicago ($51mm, IL) was sold to Northbrook Bank and Trust Company ($1.2B, IL). Northbrook gets 1 branch, all deposits (.50% premium) and virtually all assets (84% under loss share).

Exec Comp

Today, the FDIC is expected to propose that top management at banks with more than $50B in assets have 50% of their bonuses deferred for 3Ys in order to better match risk and reward.

OD Fee Suit

BofA will pay $410mm to settle a class action lawsuit over OD fees relating to disclosure and methodology.

Cash Management

The latest data finds 25% of retail transactions are still done in cash.