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BritishBusinessBank

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Enterprise Finance Guarantee

Lender Manual

2014

Contents

1 Introduction ... 5
1.1 The Enterprise Finance Guarantee ... 5
1.2 Key Manual Updates ... 7
1.3 Other EFG Guidance Available to Lenders ... 9
1.4 Enquiries ... 9
1.5 Service Level Agreement ... 10
1.6 Feedback ... 10
1.7 Continuity in Event of Scheme Closure ... 10
2 Borrower Eligibility ... 11
2.1 Introduction ... 11
2.2 Quick Reference Guide ... 12
2.3 Viability ... 13
2.4 Security ... 14
2.5 EFG Specific Tests ... 18
2.6 Eligibility Flow Chart ... 28
2.7 Eligibility Examples ... 29
3 EFG Types ... 32
3.1 Introduction ... 32
3.2 The EFG Type Decision ... 33
3.3 Type A – New Term Loan with No Security ... 34
3.4 Type B – New Term Loan with Partial Security ... 36
3.5 Type E – Revolving Credit Guarantee ... 39
3.6 Type F – Invoice Finance Guarantee ... 47
3.7 Type C – New Term Loan for Overdraft Refinancing ... 54
3.8 Type D – New Term Loan for Debt Consolidation or Refinancing ... 57
3.9 Type G – Revolving Credit Refinance Guarantee ... 68
3.10 Type H – Invoice Finance Refinance Guarantee ... 71
4 EFG for CDFIs ... 75
4.1 Policy Summary ... 75
4.2 Frequently Asked Questions ... 76
4.3 Worked Examples ... 79
4.4 Mixing Eligible and Non-Eligible Funding Sources ... 82

4.5 Use of CITR and EFG ... 82
5 The EFG Application Process Using the EFG Web Portal ... 84
5.1 Quick Reference Guide ... 84
5.2 Different EFG States and the Web Portal ... 86
5.3 Typical EFG Application Process ... 87
5.4 Adjusting Facility Details Prior to Loan Drawdown ... 93
5.5 20 Day Response Target ... 94
6 Managing EFG Facilities once the Guarantee is in Place ... 96
6.1 Refinancing EFG Debt from Another Lender ... 96
6.2 Refinancing of Non-EFG Debt from Another Lender ... 98
6.3 Changing Legal Status of the Borrower or Facility Purpose ... 98
6.4 Adjusting Facility Details Once Guarantee is in Place ... 99
6.5 Payment of the EFG Guarantee Premium ... 101
7 EFG Demands and Recoveries ... 106
7.1 Overview ... 106
7.2 Key Stages in the Demands and Recoveries Process ... 106
7.3 Worked Examples of EFG Default Scenarios ... 122
7.4 Demands & Recovery Procedure – Flowchart ... 138
7.5 Key Differences in Demands and Recoveries Rules for EFG and SFLG ... 140
7.6 The Claim Limit ... 148
8 General Information for Lenders ... 155
8.1 Annual Lending Limits ... 155
8.2 Transferring Rights and Change of Ownership ... 155
8.3 Leaving the EFG Programme ... 156
8.4 The Lender Audit Programme ... 156
8.5 Enhanced Audit ... 160
8.6 Annual Reports ... 162
8.7 Non-Compliance with EFG Scheme Rules ... 162
8.8 External Service Level Agreement ... 162
8.9 Data Protection Act ... 162
8.10 EFG Web Portal Rights ... 163
8.11 Marketing and Promotion ... 163

9 Appendices 164
9.1 Sample Data Protection and Disclosure Declaration Letter 164
9.2 Sample State Aid Letter 165
9.3 Sample Premium Payment Schedule 167
9.4 Sample Information Declaration 169
9.5 Notes on Industrial Sector Restrictions 172

Legal Disclaimer

The Enterprise Finance Guarantee (EFG) is delivered by the British Business Bank on behalf of the Department for Business, Innovation & Skills.

The British Business Bank programme is currently run directly by the Department for Business, Innovation and Skills and is not authorised or regulated by the Financial Conduct Authority or the Prudential Regulation Authority. Once HM Government has received European Commission State Aid clearance, which is expected in 2014, this programme will be transferred in its entirety to the British Business Bank plc, which will operate as a Government-owned financial institution.

Standing of Lender Manual with regard to Scheme Legal Agreement

The Lender Manual is a Scheme Document within the meaning of that term in the Legal Agreement. However, it is intended to be advisory in nature and so in the event of an inconsistency between any provision of this Lender Manual and the provisions of the Legal Agreement, the Legal Agreement shall prevail.

1 Introduction

1.1 The Enterprise Finance Guarantee

The Enterprise Finance Guarantee ("EFG") was launched in January 2009 as a successor to the Small Firms Loan Guarantee scheme ("SFLG"). The EFG is a Government guarantee scheme, delivered via accredited lenders (the "Lenders") and focussed upon improving access to working capital and investment funding for SMEs in the UK. EFG is periodically refreshed to ensure it remains relevant to the needs of Lenders and their SME customers, most recently in late 2013 and early 2014 with the relevant changes effective from 1st April 2014.

EFG can be used to **facilitate new lending** or, in certain circumstances, **refinancing of existing debt** of an SME where a Lender considers the SME viable but lacking the security normally required by the Lender.

EFG lending can support lending via **term loan, overdraft (or other permitted "revolving credit" facility) or an invoice finance facility**.

EFG may only be used to facilitate the provision of finance in cases where such finance **would not otherwise have been made available** on the grounds that the SME is unable to provide some or all of the security the Lender would normally require. For the avoidance of doubt, in refinancing scenarios the inability to provide security is understood to extend to situations in which the Lender has had reason to reassess the strength of a Borrower's existing security and, based on their normal commercial criteria, has found it to have deteriorated. Subject to all eligibility criteria being met, the EFG provides the Lender with a 75% guarantee on the net loss (i.e. after any recoveries) in the event that the borrowing SME defaults. By using EFG, the Lender is agreeing to bear the remaining 25% of any loss. **The Borrower remains liable for repayment of 100% of the outstanding debt at all times.**

The Government's total exposure to any individual Lender's annual portfolio of EFG-backed lending is capped but at a level well above the portfolio default rate most Lenders would expect to experience in their SME lending. This cap is currently set at a maximum 20% portfolio default rate, resulting in a Claim Limit upon the government guarantee equivalent to 15% of the value Lender's annual portfolio of lending (being the 20% portfolio default rate multiplied by the 75% guarantee rate).

Delivery of EFG, including the decision on whether or not it is appropriate to use in connection with a specific lending transaction, is fully delegated to the participating Lenders. **There is no automatic entitlement to receive an EFG-backed facility even if a business believes it satisfies the basic eligibility criteria.**

All of the main High Street banks plus a number of other lending institutions are participating in EFG. A list of participating Lenders is available from the website of the Department for Business, Innovation and Skills ("BIS") – https://www.gov.uk/understanding-the-enterprise-finance-guarantee and https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/209711/efg-backed-loan-application-process-and-list-of-lenders.pdf.

British Business Bank Ltd ("BBB") BBB, acting on behalf of the Secretary of State for the Department for Business, Innovation and Skills, is the principal contact point for all Lenders for EFG policy and operational matters.

1.2 Key Manual Updates

The key updates in this fourth issue of the Lender Manual are as follows:

Issue	Description	Section
Legal Disclaimer	Standard disclaimer regarding operation of the British Business Bank as a part of BIS pending EC State Aid clearance.	Preamble
Continuity in Event of Scheme Closure	Introduction of a "Parachute Clause" to enable Lenders to make alternative arrangements in the event of notification of scheme closure or material redirection.	1.7
Businesses in Difficulty	Introduction of test to ensure that EFG is not used to support a business which is in difficulty	2.3
Definition of an "Undertaking"	Revised treatment of group's to extent definition to include entities linked on a *de facto* basis.	2.5.1
Maximum Facility Amount	Maximum facility amount increased to £1.2m, subject to loan term.	2.5.2
De Minimis Regulations	The implications and implementation of changes to the EU-wide De Minimis State Aid Regulations which came into force on 1st January 2014 and will be implemented for all Offers made from 1st April 2014.	2.5.2
Mezzanine and Equity Funding	Additional clarification provided regarding use of EFG in debt for equity transactions.	2.5.6
Share Transfer Eligibility	Further clarification on use of EFG to support share transfers.	2.5.7
IHRP Standstill Arrangements	Additional guidance for Lenders who have agreed with the FCA to conduct a review of the sale of interest rate hedging products to SME customers.	2.5.8
EFG 'Type' Decisions	Decision tree to guide Lenders to the appropriate EFG Type, depending on whether the facility is new or a refinance and the debt instrument to be guaranteed.	3.2

Re-design of Type E (formerly Overdraft) EFG	Incorporates a broadening of the scope to extend use of Type E EFG to include other revolving facilities in addition to overdrafts and implementation of design enhancements to better align with Lenders' operational practices.	3.5
Re-design of Type F (Invoice Finance) EFG	Design enhancements to better align Type F EFG with Lenders' operational practices.	3.6
Enhancements to Type C (Overdraft Hardcore to Term Loan) EFG	Relaxation of conditions constraining the use of Type C EFG, primarily removing a requirement for Lenders to advance additional funding as part of providing a Type C EFG facility.	3.7
Introduction of Type G EFG - Overdraft (or other Revolving Credit) Refinance Guarantee	New EFG Type to enable Lenders to use EFG to continue providing a Borrower's existing revolving facility where an element of the facility is no longer an acceptable commercial risk and the facility would otherwise be reduced or withdrawn.	3.9
Introduction of Type H EFG - Invoice Finance Refinance Guarantee	New EFG Type to enable Lenders to use EFG to continue maintain provision of a Borrower's Invoice Finance facility where an element of the facility is no longer an acceptable commercial risk and the facility would otherwise be reduced.	3.10
Guarantee Settlements	Guidance on the treatment of 'full and final' settlements across multiple Lender guarantees.	7.2
Individual Voluntary Arrangements	Clarification of the treatment of IVR involving PPR proceeds.	7.2
PPI Mis-selling Proceeds and Business Loan Repayment Insurance	Clarification of the treatment of settlements from the mis-selling of PPI in EFG recovery situations.	7.2
Post-Claim Limit Recoveries	Guidance on the treatment of post-Claim Limit recoveries.	7.2
Small Lender Claim Limits	Introduction of two measures to encourage designated 'Small Lenders' to utilise EFG.	7.6

External Communications and Marketing	Lenders responsibilities regarding representation of EFG.	8.11
Appendices	Current versions of all Appendices included.	9

1.3 Other EFG Guidance Available to Lenders

The following guidance is also available from BBB on request:

- EFG Legal Agreement
- EFG Web Portal Manual – Version 3 of November 2012. The EFG Web Portal is the primary means of interaction between the Lender and BBB and this interaction is conducted via a secure encrypted web based portal.
- EFG Web Portal Manual Supplement dated April 2014.
- Guidance Note on Revised Premium Collection Arrangements for SFLG and EFG Schemes – Revised in February 2012.
- EFG Key Messages Document – Revised in April 2014.

1.4 Enquiries

Whilst BBB welcomes enquiries from Lenders, the intention is that the vast majority of enquiries can be adequately answered by reference to the Lender Manual, the Web Portal Manual and/or Web Portal itself.

When seeking to deal with unusual situations Lenders are encouraged to begin by asking the question "if EFG did not exist, what would be our approach to tackling this situation according to our normal commercial criteria and guidelines."

Please note that BBB would usually expect enquiries to come via the Lender's Principal EFG Contact rather than directly from Relationship Managers, as for RMs the source of responses to their queries should be the Principal EFG Contact.

Enquiries arising from perceived shortcomings in the content of the Manual, or instances where other published material appears to contradict the Manual, are welcome.

Brief, simple enquiries can be made via the "Ask BBB" function on the Web Portal (see Web Portal Manual v.3 section 5.5). For more detailed or complex queries, please use the Web Portal function to alert BBB that a more detailed email will follow.

1.5 Service Level Agreement

BBB recognises that Lenders value swift responses to queries and will use reasonable endeavours to respond to any Lender query within 3 business days. Where a query is complex and requires more time, this will be explained to the Lender. Where a query requires referral to a third party, resolution may take longer than the stated 3 business days. In such instances BBB commit to refer the query to the third party within a period of 3 business days. BBB will attempt to seek a speedy resolution to the issue thereafter but may ultimately be reliant upon third parties in these instances.

1.6 Feedback

Feedback on potential improvements or amendments to EFG design or processes is formally solicited during the audit process (covered in Section 8.4). Nevertheless, BBB welcome feedback on any aspect of EFG design at any time.

1.7 Continuity in Event of Scheme Closure

In the event that a decision were to be made to close the EFG scheme to new lending then any lending agreed prior to the closure date remains covered by the guarantee without change.

In addition, and particularly relevant to the overdraft, revolving facility and invoice finance options, a "parachute clause" in the scheme Legal Agreement allows the Lender to reassess the status of each such facility so that, if necessary, an appropriate replacement EFG-backed facility may be provided prior to the closure of the scheme.

2 Borrower Eligibility

2.1 Introduction

There are three central criteria to EFG eligibility:

1. **Viability**: The Lender must be of the opinion that the Applicant can viably service and repay the proposed debt, assessed according to the Lender's normal commercial credit policies. The purpose of the scheme is to facilitate lending to SMEs which would not otherwise be possible due to lack of security. It is not a mechanism for "propping up" an SME which is ultimately incapable of servicing a loan or for a Lender to shift risk from its own balance sheet to the Government (see section 2.3 for more detail);

2. **Security**: The Lender must have assessed the availability of security according to its normal commercial criteria and has established that insufficient security is available to meet its normal lending criteria. The Lender must declare that it would have be prepared to offer the Applicant finance if more collateral had been available (see section 2.4 for more detail); and,

3. **EFG Specific Tests**: EFG is aimed at UK SMEs. The tests relate to business size and sector, loan amount and term. Restrictions apply for certain industrial sectors and activities (see section 2.5 for more detail).

Note that, even if credit sanction for a proposed EFG facility has been granted internally by a Lender, eligibility for EFG can only be confirmed once the Applicant and their proposition have been confirmed as eligible via the Web Portal.

2.2 Quick Reference Guide

Criteria	Description	Manual Reference
Viability	The Lender believes that the Applicant has a viable borrowing proposal and that the EFG facility can be serviced and repaid	2.3
Businesses in difficulty	The Lender confirms that the Applicant is not in insolvency proceedings, not does it meet the criteria for being placed in insolvency proceedings at the request of its creditors	2.3
Security	The Lender would be prepared to offer the Applicant finance if more collateral was available. Security can be charged alongside the EFG facility. All forms of security are eligible other than Principal Private Residence ("PPR")	2.4
Maximum turnover	Group sales must not exceed £41m	2.5.1
Amount	£1k to £1.2m, subject to *de minimis* limits and the proposed loan term.	2.5.2
Term	Term loan: 3 months – 10 years (5 years for lending over £600k) Overdraft (and other permitted "revolving facilities"): 3 months – 3 years Invoice Finance: 3 months – 3 years	2.5.3
Industrial sector	Most sectors are eligible. Coal is ineligible, whilst partial restrictions apply to agriculture, fish farms, insurance, banking, formal education and road transport	2.5.2
Exports	Restrictions apply in certain circumstances where export-related activities are to be financed	2.5.5
Share transfers	Funding acquisitions may be eligible for EFG, provided that there is clear benefit to the business and the lending it to a trading entity and not an investment vehicle or individual	2.5.7

2.3 Viability

Evaluation of the Applicant's viability is devolved to each Lender, which must use its normal commercial lending criteria to appraise each proposal. The Lender may proceed if:

- the Lender believes that the Applicant has a viable business plan and that the EFG facility can be serviced and repaid;
- the Lender would be prepared to offer the Applicant finance if more collateral was available; and,
- the Lender believes a term loan, overdraft or invoice finance facility is the appropriate debt instrument to use in terms of the Applicant's finance raising.

SMEs which have defaulted on historic EFG (or SFLG) schemes are not disqualified from applying for EFG (assuming all normal eligibility criteria are met). The individual lending decision is at the discretion of the Lender.

However, EFG should not be used as a mechanism for a Lender to shift risk from its own balance sheet to the Government.

"Business in Difficulty" Test

There is a requirement to ensure that EFG is not used to provide support to a business which is in difficulty, being described in the scheme Legal Agreement as "a Business which is unable, whether through its own resources or with the funds it is able to obtain from its shareholders or creditors, to stem losses which, without outside intervention by the public authorities, will almost certainly condemn it to going out of business in the short or medium term". This definition is consistent with the relevant legislation which permits BBB to offer the EFG scheme to Lenders.

In practice it is expected that Lenders' own commercial criteria will eliminate propositions from Applicants which have no realistic prospect of survival. Where finance is to be provided as part of a planned restructuring of a business, then it is expected that the Lender will have established that all parties with an interest in the business are committed to a successful outcome, such that the business does not represent a "business in difficulty" as defined in the scheme Legal Agreement. For the avoidance of doubt, in such situations the basis on which EFG may be used by the Lender remains unchanged – that the proposition is sound but for the inadequacy of the Applicant's security.

This will require the Lender to answer a simple narrative statement on the Web Portal requiring selection of a "Yes" or "No" see Web Portal Manual Supplement issued April 2014.

2.4 Security

The rules regarding security are as follows:

1. **<u>The Lender should investigate all available security and either charge it or discount it as unavailable, according to its normal credit and security assessment procedures.</u>**

Definition of security: All business or, if appropriate, personal assets which a Lender would look to as security for business borrowing in the normal course of business.

- For sole traders and partnerships, Lenders should investigate the personal assets of the individuals owning the business in accordance with normal commercial practice.
- For a limited company, potential security would generally include all standard business security (for example, fixed charges, debentures, corporate guarantees), plus Personal Guarantees from directors / shareholders / third parties where appropriate.
- Personal Guarantees may be Supported or Unsupported, as deemed appropriate by the Lender.
- Unsupported Personal Guarantees from a director / shareholder are frequently viewed as a means of demonstrating personal commitment by the individual(s) concerned to the business and so a Lender is entitled to request such security if to do so is consistent with the Lender's normal commercial lending criteria.
- For Supported Personal Guarantees, Lenders can look to any personal asset of the Guarantor other than their Principal Private Residence (PPR). Charging a PPR is strictly prohibited for EFG.
- **Lenders should make Borrowers aware that, in the event of default, the Borrower remains liable for 100% of the outstanding EFG debt and that normal recovery and enforcement procedures (against the Borrower (and Guarantor(s) where applicable) will be pursued by the Lender before any demand is made on the scheme guarantee. The provision of the EFG guarantee does NOT remove any liability for the borrowing from the Borrower or Guarantor.**

Having examined all potentially available security, the Lender will in effect find that one of four security scenarios applies:

1. The Lender believes the Borrower has **sufficient security** available to secure the borrowing requirement. By definition, the borrowing requirement can be funded via a standard secured commercial facility and EFG does not need to be used.

2. The Lender believes the Borrower has **no security** available to secure the borrowing requirement. Consequently, the borrowing requirement cannot be met using a secured facility unless security is available from another source, i.e. the EFG guarantee. Therefore, in these circumstances, EFG **can** be used to support the full borrowing requirement.

3. The Lender believes the Borrower has **some security, but that this is insufficient** to fully secure the borrowing requirement. In these circumstances, EFG **can** be used to support the full borrowing requirement provided that the Lender also charges all the other security identified as being available in support of the borrowing alongside the EFG guarantee and identify it appropriately in the facility letter. Such additional security is referred to as "Linked Collateral" for EFG purposes. In the event of Borrower default, any proceeds realised from this Linked Collateral must be used to repay this specific debt in priority to any other outstanding debt and before making a claim against the EFG guarantee.

4. Alternatively, where the Borrower has **some security but this is insufficient** to fully secure the full borrowing requirement the Lender may provide secured commercial lending to the maximum extent possible considering the security available and then **make up the shortfall** in the borrowing requirement **with a separate EFG-backed facility**.

The Lender has complete discretion on which funding approach to adopt and may follow different approaches in different cases.

Whenever EFG is to be used, the Lender must be able to confirm that, but for a lack of security, it would otherwise lend to the Borrower. The Lender makes a declaration to this effect.

Security previously taken by a Lender may be released during the life of a loan provided that it is consistent with normal commercial procedures for the Lender to do so, and that details of the justification for the release of any security is kept on the Borrower's file (by way of a credit application or some other documentation as appropriate to the Lender) for potential audit purposes. **The release of any security to deliberately transfer risk from the Lender to Government, or to strengthen the Lender's position in respect of another facility if it appears that the Borrower may be in difficulty is a misuse of the scheme**.

Please note that it is not the Borrower's right to demand an EFG-backed loan. If the lender does not believe that any particular form of finance is suitable for a Borrower (other than because of an inadequacy of security) then EFG does not make it suitable. If, however, due to a lack of security a Lender would find it necessary to offer a Borrower a form of finance other than that which is considered the most appropriate (e.g. invoice finance in place of a term loan for working capital), then EFG may provide the means to enable the provision of the term loan. Nevertheless, in all cases the decision to use EFG, and the lending instrument it is used with and the terms of the finance provided, are always at the discretion of the Lender.

2) <u>For EFG, Principal Private Residences (PPRs) are excluded as potential security</u>

The only type of security which receives a treatment under EFG which may differ from the Lender's normal commercial practice is the Principal Private Residence ("PPR") of a Borrower or Guarantor. This reflects the clear view of Ministers that they wish to avoid the possibility of individuals losing their homes as a result of having personally guaranteed borrowings to businesses in receipt of EFG-backed borrowing. With the exception of the PPR restriction, any other specific inclusions or exclusions are those arising from the Lender's own security policies.

Areas for Lenders to consider:

Is there equity in the PPR? If so, is the Borrower or Guarantor willing to provide a charge over the PPR?

- If a Borrower or Guarantor has equity in their PPR (sufficient to fully or partially secure the borrowing requirement), a Lender needs to ascertain the willingness of the Borrower or Guarantor to provide a charge over the PPR (as per their normal security assessment procedures).
- If the Borrower or Guarantor is willing to provide a charge over the PPR, then the Lender has the option of addressing the funding requirement which is capable of being secured in that way via a normal commercial facility. Any additional funding requirement thereafter could potentially be provided by EFG-backed lending.
- Where the Borrower or Guarantor is **unwilling** to provide a charge over the PPR, then it is **the Lender's decision** whether to:

    - Accept the Borrower and / or Guarantor's stance (and thus accept that the PPR is beyond consideration). In this instance, use of EFG will be permissible. The Lender should keep a note on file providing a clear explanation as to why the Applicant's refusal to provide security was accepted. This is NOT to be viewed as a mechanism for transferring risk from the individual or the Lender to the scheme;

  or,

    - Decline the funding request (and refuse to consider the possible use of EFG) on the grounds that there was security available but the Borrower and / or Guarantor refused to make it available.

For the avoidance of doubt: Under no circumstances can a PPR be taken as security (directly or indirectly) for an EFG-backed facility.

- In a recovery scenario (where the PPR has not been charged but, because there are other debts in respect of which a guarantee from which a link can ultimately be established through to the PPR, the Lender wishes to pursue this asset via a charging order), any funds subsequently realised from this action **cannot** be applied to reduce outstanding EFG-backed exposure.
- Even though a PPR cannot be taken as security in respect of EFG-backed lending, a Lender should assess whether a refusal by the Applicant to provide a charge over a PPR to support a normal commercial loan is reasonable. An unwillingness to provide it may in some circumstances be interpreted as the Applicant's lack of commitment to, or confidence in, the project to be funded and thus inform the commercial decision to lend.
- Similarly, where a Borrower or Guarantor appears to have access to security other than his / her PPR (e.g. an investment property, boat, etc.) but refuses to charge that asset to the Lender, or where the asset is held jointly with another (often the spouse) and they argue that the asset cannot be offered as security because the co-owner refuses to give permission, it is the Lender's decision on whether to accept the Borrower or Guarantor's request to exclude such assets from consideration in making a lending decision, and any decision on that issue in respect of EFG-backed lending must be demonstrably consistent with the Lender's normal commercial decision-making for such situations
- **The existence and eligibility criteria of the EFG should not be seen by Borrowers or their advisors as a mechanism for putting personal assets which might normally be considered as security beyond consideration, nor should a Lender entertain use of EFG in this context.**

Mixed use property

- In the event that a property is used as both a residence and a business location (such as a flat above a shop for which there is a single title deed) by a Borrower or Guarantor then, for EFG purposes, the property is deemed to be a PPR. As such, for an EFG facility, the Lender cannot charge this asset or call upon it in the course of a security and recoveries process.
- However, if the property is the subject of a mortgage independent of the EFG facility and that mortgage is not being serviced in accordance with the terms of the agreement, then the fact that the Borrower also has an EFG facility does not affect the Lender's ability to follow their normal course of action in respect of pursuing the breach of the mortgage terms.
- In summary, a mixed use property which is a Borrower's or Guarantor's PPR can be viewed and used as standard security for normal commercial lending but cannot be used to secure EFG lending.

2.5 EFG Specific Tests

2.5.1 Group Turnover Limit

Lending to businesses, not individuals unless the individual is a sole trader

EFG is to support businesses and not personal lending. Therefore, EFG loans cannot be made to company directors in their personal names for investing into a limited company. EFG loans can be made to sole traders, partners and limited companies BUT lending cannot be made to individuals in a personal capacity. For the avoidance of doubt, sole traders are expected to produce financial accounts to demonstrate their trading activities.

Maximum group sales of £41 million

The maximum annual turnover of the Applicant (or Applicant's group) must be no more than £41m. The source of the turnover figure should be the latest management or statutory accounts, whichever is deemed appropriate according to each Lender's normal credit assessment criteria.

For start-ups, or businesses which have traded for less than 12 months, the turnover figure should be the forecast outturn for the first 12 months of trading.

Groups and common directors

An "undertaking" is defined as any entity engaged in economic activity, regardless of its legal status and the way in which it is financed. All entities controlled (on a legal or *de facto* basis) by the same entity are considered to be a single undertaking and thus constitute a group. Each undertaking is subject to the same single maximum permissible aid ceiling.

Where the Borrower is an entity within a larger undertaking, aggregated turnover for the whole group should be used to assess the Applicant's sales.

UK domiciled business

Businesses which are owned by foreign parents are eligible to apply for EFG provided the Applicant is trading in the UK and the EFG-backed funding is deployed into a business activity in the UK.

Similarly, where a business has UK ownership but is registered abroad, the business is eligible to be considered for EFG-backed borrowing provided the Applicant is trading in the UK and the funding is going towards a business activity in the UK. The "core" of a business' operations must be in the UK.

2.5.2 Amount of EFG Facility

EFG guarantees are available for a minimum facility of £1k and a maximum of £1.2m (previously £1m).

However, where an EFG-backed term loan facility has an initial term in excess of 5 years (and up to the maximum term of ten years) a reduced maximum facility amount of £600k applies, reflecting the requirements of the *de minimis* State Aid regulation.

Lenders are free to set higher minimum and lower maximum thresholds for their use of EFG, in accordance with their own lending product specifications and market positioning, subject to such limits falling within the above parameters.

All lending must be made in pounds sterling.

£1.2m outstanding facility limit for EFG

As of 1st April 2014, there is a maximum £1.2m outstanding facility limit for EFG. No Borrower may have more than £1.2m of outstanding guaranteed term loan debt or guaranteed overdraft or invoice finance facilities available for use (or a combination amounting to £1.2m in aggregate) at any one time. Applicants may benefit from more than one EFG-backed facility so long as the aggregate outstanding at any one time does not exceed £1.2m.

Each individual EFG-backed facility must comply in turn with the rules governing facility amount and term, such that if all lending has an initial term of over 5 years the maximum outstanding facility limit would effectively be reduced to £600k.

€200,000 rolling three-year State Aid limit

The assistance provided through EFG, like many Government-backed business support activities, is regarded as State Aid and is governed according to the European Commission's *de minimis* State Aid regulations. To comply with these the total value of the applicant's *de minimis* State Aid for the most recent three years (including that arising from the current EFG application) must be no more than €200,000, or the relevant lower threshold where advised for restricted industries as set out in the table below. Further guidance regarding restricted sectors is available in Appendix 9.5. It should be noted that this guidance is correct as at the date of publication, and is subject to change.

	Maximum Amount	**Maximum Guarantee Term**
Applicant carrying on Business in any eligible sector save for the Road Freight Transport sector, the Agriculture sector or the Fisheries sector	£1,200,000	5 years
	£600,000	10 years
Applicant carrying on Business in the Road Freight Transport sector	The lesser of (1) £1,200,000 and (2) such amount as would result in the aggregate *de minimis* State aid being made available to the Applicant equalling €100,000, as calculated by the Scheme Website Application Process	5 years
	The lesser of (1) £600,000 and (2) such amount as would result in the aggregate *de minimis* State aid being made available to the Applicant equalling €100,000, as calculated by the Scheme Website Application Process	10 years
Applicant carrying on Business in the Agriculture sector	The lesser of (1) £1,200,000 and (2) such amount as would result in the aggregate *de minimis* State aid being made available to the Applicant equalling €15,000, as calculated by the Scheme Website Application Process	5 years
	The lesser of (1) £600,000 and (2) such amount as would result in the aggregate *de minimis* State aid being made available to the Applicant equalling €15,000, as calculated by the Scheme Website Application Process	10 years

Applicant carrying on Business in the Fisheries or aquaculture sectors	The lesser of (1) £1,200,000 and (2) such amount as would result in the aggregate *de minimis* State aid being made available to the Applicant equalling €30,000, as calculated by the Scheme Website Application Process	5 years
	The lesser of (1) £600,000 and (2) such amount as would result in the aggregate *de minimis* State aid being made available to the Applicant equalling €30,000, as calculated by the Scheme Website Application Process	10 years

The amount of State Aid received by the Borrower is calculated via the Web Portal based on loan value and term on a pro rata basis.

Verification of Borrower's State Aid

As part of the appraisal process the Lender must ask the Applicant to confirm that receipt of the EFG-backed facility will not result in the Applicant breaching the £1.2m outstanding facility limit for EFG or the rolling three-year €200,000 State Aid limit (or lower limit where a restricted industry is concerned). The Lender may accept the Applicant's declaration as being sufficient confirmation of this point. However, should the Lender have any reason to believe that the Applicant may in fact be in breach of the limits, there is a duty upon the Lender to make further enquiries which may ultimately lead to rejection of the Application.

If a Borrower is found to be in breach of the limits once the loan has been drawn, the Lender must cancel the EFG facility by marking the loan as "No Claim" on the Web Portal (see Web Portal Manual v.3 section 11.3). It will be a commercial decision for the Lender whether or not to permit the facility to continue (without the guarantee) from that point.

Restricted industries

EFG may not be used to facilitate lending to businesses operating in the following sectors:

- Coal
- Banking, finance and associated services (except professional services)
- Formal education (except vocational training)
- Insurance and associated services (except brokers and agents)
- Public administration, national defence, and compulsory social security

Further information on these restricted industries is available at Appendix 9.5.

The EFG Web Portal calculates the amount of State Aid (see Web Portal Manual v.3 section 8.3) and advises whether, taking account of the Aid arising from the EFG facility and any previous aid declared by the Borrower, the threshold has been breached. Where restricted sectors are concerned, from 1st April 2014 the Web Portal will apply the lower threshold in the test. BBB will periodically investigate potential breaches of the *de minimis* rules and the EFG may be withdrawn on loans where State Aid limits have been exceeded.

Lenders should use the Web Portal to check for eligibility and, where explanation is necessary, additionally refer to Appendix 9.5 to establish whether any of the lower limits apply. Eligibility should be checked at the earliest opportunity in order to avoid any potential wasted effort by the Lender or Applicant.

It should be stressed that the overarching principle with regards to selecting the most appropriate industrial sector is the specific activity to which the EFG backed finance is to be applied. If a business is active in a number of sectors, including some restricted sectors, EFG can still be used if the funds are specifically for investment, working capital or refinancing in a qualifying sector. In this instance, when entering the SIC code on the Web Portal, the SIC code selected should be that of the qualifying sector to which the funds are being applied (more information on entering SIC codes on the Web Portal is available in the Web Portal Manual v.3 section 7.2).

2.5.3 Facility Term and Margin

The maximum permissible term parameters are as follows:

- **EFG term loan** – between three months and ten years (subject to compatibility of loan amount);
- **EFG overdraft and other revolving facilities** – between three months and three years; and,
- **EFG invoice finance facility** – between three months and three years.

More details with regards to each type of facility can be found in the relevant parts of section 3 of this Manual.

Repayment options

For all types of EFG, the Lender has the option to require:

- Regular repayments (monthly, quarterly, annually at discretion of Lender) over the facility term; or,
- Bullet repayment at expiry (in which case, the Lender's assessment must include consideration of the Borrower's capacity to make repayment, either outright or via a refinance at expiry).

Capital repayment holidays

Capital repayment holidays ("CRH") are permissible but are at the discretion of the Lender and must comply with the Lender's standard credit procedures.

In all instances, the EFG facility must still be fully repaid within ten or three years (including, for the avoidance of doubt, this being achieved by a series of lump sum repayments or a single bullet repayment on maturity), depending on the EFG Type used by the Lender.

Tranche drawdowns and facility availability period

The Lender can allow the Borrower to draw down the EFG facility gradually, as and when it is needed. However, in the event of staged draw down, the first tranche must be drawn down within six months of the EFG facility being offered, or within the standard timeframe applied by the Lender, whichever is shorter.

Upon initial drawdown, the Lender must update the Web Portal within 10 business days of the drawdown. It is the Lender's responsibility to keep the Web Portal up-to-date at all times, including where drawdown or repayment has occurred.

In the event that a Borrower decides to use subsequent tranche drawdowns for a different purpose than that originally stated, the Lender must consider whether the facility is still eligible for EFG (see section 6.3.2).

Arrangement fees and interest rate margin

The Lender may charge an arrangement fee and price the interest rate margin for the EFG facility in accordance with their normal pricing policies.

2.5.4 EFG Purpose

EFG purpose

EFG can be used in a qualifying sector for:

- investment;
- working capital; or,
- refinancing.

2.5.5 Exports

Restrictions on EFG for exporting

As EFG operates under the *de minimis* State Aid regulations it cannot be used to specifically support export-related activities. This is because public support for exporting is particularly sensitive from a competition perspective and so is covered by separate EU agreements. This does not mean, however, that because a business exports it is automatically ineligible from receiving an EFG-backed loan. It is the purpose to which the borrowed funds will be put which is the determinant.

EFG applications will be ineligible if the purpose of the funding is specifically linked to a quantity of goods or value of services being exported. Therefore, a facility to provide working capital specifically in support of export sales will be ineligible because working capital requirements are usually driven by sales orders.

In addition, Lenders need to consider whether the funding is in support of **dedicated export activities or to promote exports**. Further **ineligible** purposes include, for example, the financing of:

- an advertising campaign outside the UK;
- an individual export order;
- the manufacture of a product which is only available to customers in an overseas market;
- the establishment of a representative office outside the UK or the appointment of an overseas agent; and,
- the setting up of a distribution network overseas.

Activities not directly related to specific exports are **eligible**, including:

- participation in trade fairs, general promotion and marketing rather than in relation to an individual export order;
- feasibility studies or consultancy support to facilitate the launch of a new or existing product into a new market; and,

- specific activities (e.g. generic product development, equipment purchase or facilities enhancement activities) within the UK operations of a business, irrespective of the current composition of market(s) into which the business sells.

Care should be taken when assessing applications from SMEs serving customers which are UK-based exporters. In such scenarios, whilst the Applicant's services may be linked to export activities (e.g. provision of specialist packaging materials and/or services, obtaining of licences or other documentation necessary to facilitate export sales etc), the Applicant itself may not actually export. Such a business, subject to its industrial sector and the other eligibility criteria, may therefore be eligible for EFG-backed lending.

Protectionism

The *de minimis* rules are also designed to prevent protectionism. EFG therefore cannot be used if provision of the finance is being made conditional on the use of domestically produced goods or services in preference to imports.

2.5.6 Lenders Providing Mezzanine and Equity Funding

A Lender cannot generally lend to an Applicant with the backing of EFG if the Lender also holds an equity interest in the Applicant.

The exception to this rule is where:

- equity has been taken previously in exchange for write-off of debt and the EFG facility is provided more than two years after the equity stake was taken; and

- there is clear evidence to show that the business has survived, trading performance has improved since the equity stake was taken and the business is now looking to expand; and

- the funding provided is not to be used to buy back the Lender's shares, nor must provision of the funding be made conditional on the acceptance by the Borrower of variations to any existing agreement regarding ultimate buy-back (the Lender must not sell their shareholding whilst the EFG facility remains outstanding without explicit reference to and agreement from BBB); and

- EFG **<u>cannot</u>** be used where equity is being taken in exchange for debt being written off and a separate term loan/overdraft (which the Lender was proposing to use EFG to support) is being granted at the same time.

2.5.7 Share Transfers

EFG is designed to stimulate economic growth and all EFG lending is intended to add economic value to the borrowing businesses. Share transfers (including purchases of minority interests, share buy-backs and corporate acquisitions effected via the purchase of a business' trade and assets) do not in themselves introduce new funds into a business and are often motivated by personal gain. It is not within the spirit of EFG for it to be used for the benefit of individuals rather than businesses.

Share transfers may, however, impact on corporate control and EFG may be used in support of such transactions if this is of clear benefit to the business (for example by enabling the business to expand into new markets or develop additional products, or create additional jobs etc.) The Lender must be prepared to justify any decision to the auditor, and it is recommended that Lenders prepare a file note justifying the use of EFG, where appropriate.

In Share Purchase transactions, EFG should only be used to support lending to trading entities and not to investment vehicles or individuals.

2.5.8 Interest Rate Hedging Products Standstill Arrangements

Where a Lender has agreed with the FCA to conduct a review of the sale of interest rate hedging products to SME customers is its recognised that, other than in exceptional circumstances, they will not foreclose or adversely vary existing lending facilities to customers who are within the scope of the review without giving prior notice to the customer and obtaining their prior consent.

As a consequence of this "standstill" arrangement, where the loan facility is EFG-backed the following action should be taken:

- When a customer is issued with a 'Notice of Default / Reservation of Rights letter the loan should be moved to Lender Demand on the Web Portal, which will stop further EFG premiums being collected;

- The 'Date of Demand' input on the Web Portal should be the date of the 'Notice of Default / Reservation of Rights' letter;

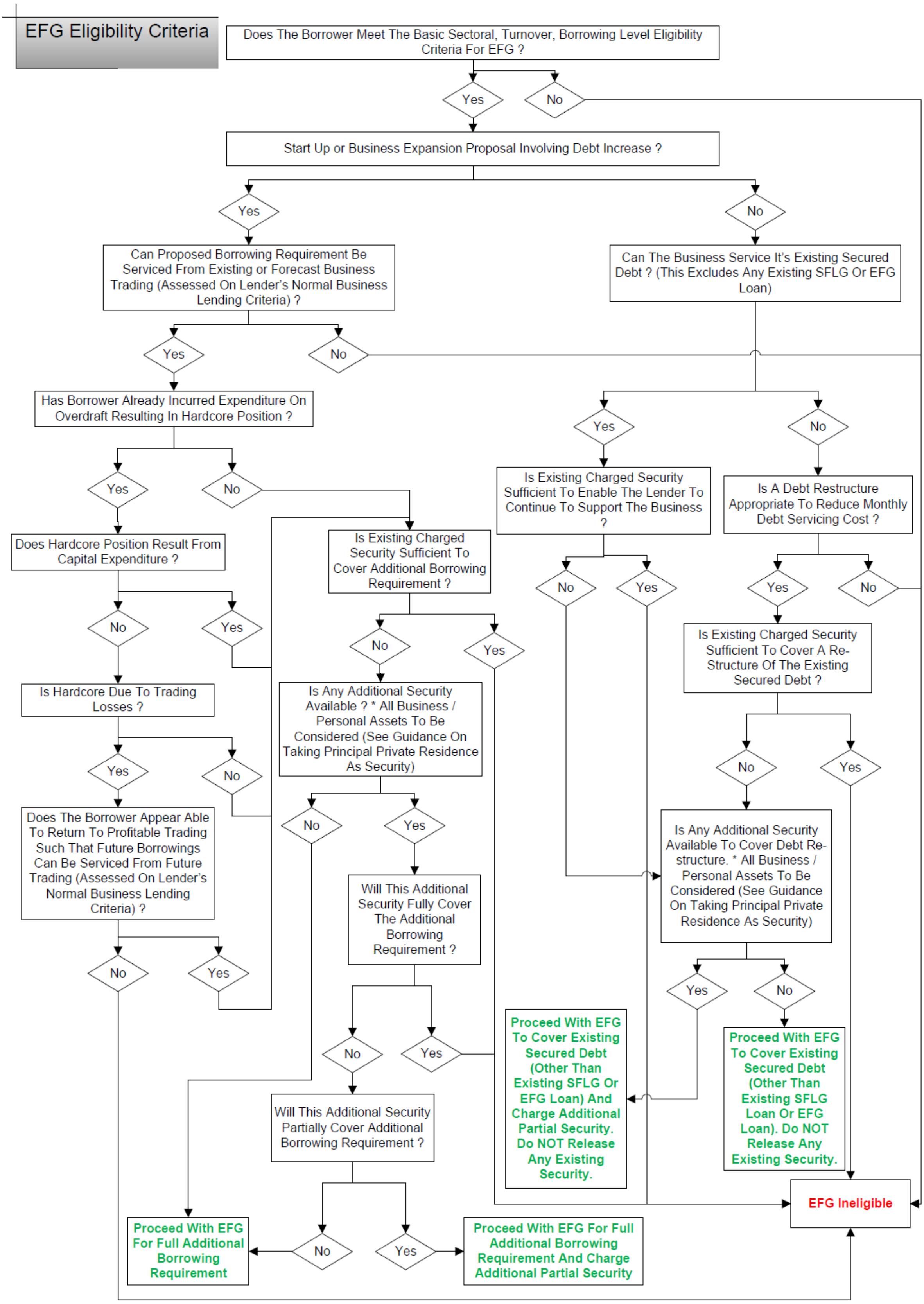
- When a determination under the review is reached the Lender should change the facility status on the Web Portal back to 'Guaranteed'. If the Lender then pursues recovery action, the facility status should be changed within five working days back to 'Lender Demand', now inputting the date of demand as the date the Lender issues the 'Demand Letter';

- This will ensure that the amount of time the Lender has to complete the Recovery process before submitting a Claim under the Guarantee is not affected by the agreement with the FCA;

- Where a customer is within scope of the review but is not in default and has not otherwise been issued with a 'Notice of Default / Reservation of Rights' letter, the loan status should remain at 'Guaranteed' with repayments and premiums being collected from the Borrower as normal.

2.6 Eligibility Flow Chart

The following chart can be used to help appraise eligibility for EFG:



2.7 Eligibility Examples

Example 1 – General Eligibility		
• The Applicant, a limited company with a turnover of over £1m per annum, is an insurance brokerage business specialising in commercial insurance products. • Mr Smith, the owner / manager has decided to expand geographically and £50k of funding (repayable over 3 years) is required to open a new office in a neighbouring town plus working capital. A business plan has been presented to the bank. • The RM thinks that the business can service the loan, and asks what security is available. The business has no chargeable assets (the new office will be on a 5-year lease). Mr Smith's personal net asset statement shows he has no material assets available, but Mr Smith says that he may be able to get his brother to offer a personal guarantee for £12.5k supported by a charge over his house – and that this will mean that the bank would be 100% covered on a £50k EFG.		
Example 1 – Appraisal		
Issue	**Eligible**	**Notes**
Viability	Yes	• The RM believes the business can service the facility, the business is not subject to insolvency proceedings and does not meet the criteria for being place in insolvency proceeding at the request of its creditors.
Security	No	• Personal guarantee is valid for EFG BUT a lender cannot take a charge over a PPR if EFG to be used. • A personal guarantee does not cover a ring-fenced 25% of the loan. • If a charge over the PPR is available, the RM should consider whether this proportion of the funding requirement could be offered via a normal commercial loan.
UK business /export restriction	Yes	• Business is UK based and expansion is not overseas
Turnover	Yes	• £1m sales
Term	Yes	• 3 years
Amount	Yes	• £50k
Sector	Yes	• Insurance brokerage (so long as not writing policies)
Summary The security offered by the Applicant, relating to the PPR, is does not appear suitable for EFG purposes. However, as the Applicant meets the viability and general EFG eligibility tests, the proposal is still potentially eligible. If, after further checks on security availability, no security is available for EFG, the borrowing proposal would be eligible for EFG support.		

Example 2 – General Eligibility
• Jolly Burger is a giant US corporation which operates thousands of fast food restaurants under franchise agreements. Mr Bloggs holds one of the Jolly Burger restaurant franchises in Birmingham (operating as Jolly Burger (Birmingham) Limited) and has approached the bank for funding to help buy the Jolly Burger franchise in Wolverhampton, as the current franchisee is retiring. • The sale price is £100k. Mr Bloggs is contributing £30k and is applying for the remaining £70k via a 5-year term loan, plus a £10k overdraft for 12 months. The debt would be in the name of a new limited company, Jolly Burger (Wolverhampton) Limited and Mr Bloggs is the sole shareholder of each company. The RM thinks that the combined business will be able to service the debt, but would normally want to see significant security for a loan such as this. • Mr Bloggs has no assets other than a share portfolio worth about £40k.

Example 2 – Appraisal

Issue	Eligible	Notes
Viability	Yes	• The RM believes the two companies can service the requested borrowing facility.
Security	Maybe	• Normal commercial practice applies: Would the Lender normally take a charge over the share portfolio? • If so, can the Lender provide some of the funding via a normal commercial loan?
UK business /export restriction	Yes	• The business being supported will be making all sales in Wolverhampton and so is a "UK business".
Turnover	Maybe	• Probably. Only use Jolly Burger's turnover if it has a controlling influence over the franchisee. In accordance with normal commercial lending practice the Lender will wish to check the terms of the franchise agreement.
Term	Yes	• 5 years / 12 months
Amount	Yes	• £70k / £10k
Sector	Yes	• Restaurant / food outlet is eligible
Business transfer	Yes	• Acquisition will enable target business to continue

Summary

Further checks need to be undertaken in order to ensure the general EFG eligibility tests are all satisfied and that there is nothing in the franchise agreement which compromises the ability to lend to the new limited company. In terms of security, even if the Lender generally takes a charge over shares, this still appears insufficient to meet a Lender's standard security requirements. Therefore, this proposal is probably eligible for EFG.

3 EFG Types

3.1 Introduction

The EFG scheme **enables** lending **to be supported** in a variety of different sets of circumstances.

EFG can be used to support lending via any combination of the following variables:

a) Type of Debt Instrument:

- Term loan
- Overdraft and other permitted revolving facilities
- Invoice finance

(all subject to being secured lending instruments)

b) Borrower's ability to provide Security:

- Some but insufficient security available
- No security available

c) Funding Requirement:

- New or increased amount of borrowing
- Refinancing (with or without an increase in borrowing)

For EFG borrowing proposals, combinations of the above variables determine the classification ('Type') of EFG facility. The EFG Lending Type is simply an administrative label and Lenders should avoid referring to specific EFG Lending Types in discussions with customers – the customer-facing message should simply be that the Lender has the means, thanks to the EFG guarantee, to offer finance in circumstances where they would otherwise have to decline it due to the inadequacy of the Applicant's security. Any differences in eligibility criteria between EFG Lending Types are covered in this chapter.

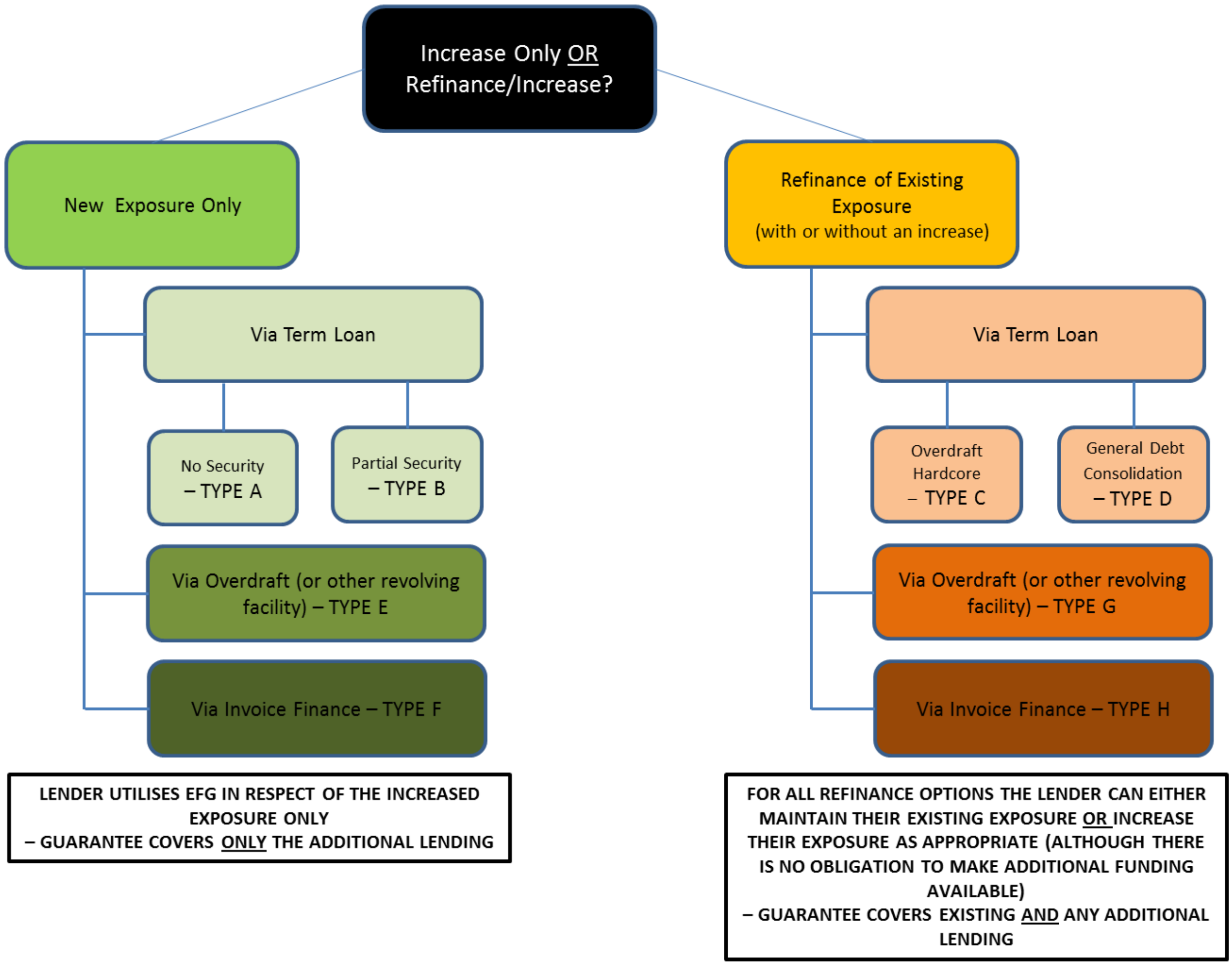
3.2 The EFG Type Decision

The decision on how the Lender should classify their use of EFG (i.e. in informal terms which EFG 'Type' a Lender should use) is determined by two key factors:

1. Is EFG to be used solely to support an increase in existing lending or is there is any element of refinancing of the Lender's existing exposure?

2. What is the type of debt instrument the Lender will be using?

The different options resulting from the Lender's responses to the above are illustrated below:



Note: Use of 'Refinance' EFG Types is limited to a maximum of 20% of a Lender's utilisation of their EFG Lending Limit Allocation.

3.3 Type A – New Term Loan with No Security

Overview

Type A EFG is used for new or additional borrowings via term loan where the Borrower is viable but has no available collateral to secure the borrowing requirement, according to the Lender's normal credit criteria.

With the possible exception of personal liability for loans to sole traders and partnerships, the only recourse the Lender has in the event of default on a Type A facility is to the government Guarantee.

If the Lender has recourse to any business assets, including via the extension of security held for commercial facilities where the Lender's assessment of security value is nil, the EFG facility is not unsecured and should **not** be input as a Type A facility but instead should be regarded as partially secured (Type B).

Eligibility Criteria

Guarantee Term:	Minimum 3 months up to maximum 10 years
Minimum Amount:	£1k
Maximum Amount:	£1.2m for loans with a term of up to 5 years £600k for loans with a term of over 5 years
Purpose:	New or additional borrowing only
Lending Product:	Term Loan
Lender Security:	Subject to the Lender's normal commercial criteria, all available security (business or personal, excluding Principal Private Residence (PPR)) should be considered to back the EFG loan.
Premium Payment:	2% per annum, quarterly in advance against outstanding loan balance

Example of Type A lending
The Application: • An existing business wishes to borrow £50k to finance a R&D project. • It currently has a commercial mortgage of £400k on a property valued at £575k, representing a LTV of 70%*, which is the Lender's maximum LTV. • No more security is available. **Note: the 70% LTV is for illustrative purposes only – normal Lender credit criteria, including specification of LTVs, will apply in all instances.*
The Outcome: • The Relationship Manager ("RM") assesses that the Applicant can afford to repay £50k over a 10-year period, assessed according to normal lending criteria. • The RM is minded, however, to decline the application because a) there is no more lending capacity in the property, which is already at the bank's maximum LTV; and b) there is no further security available. • The use of EFG to facilitate the additional funding requirement is, therefore, appropriate because the only issue preventing the approval of the Application is the lack of security.

3.4 Type B – New Term Loan with Partial Security

Overview

Type B EFG is used for new or additional borrowings via term loan where the Borrower is viable and has some though insufficient security to secure the borrowing requirement according to the Lender's normal credit criteria

Where some security (of any kind and value, including Personal Guarantees and the extension of security held for commercial lending) is being provided by the Borrower in support of the EFG facility, the application should be entered onto the EFG Web Portal as a Type B loan.

Eligibility Criteria

Guarantee Term:	Minimum 3 months up to maximum 10 years
Minimum Amount:	£1k
Maximum Amount:	£1.2m for loans with a term of up to 5 years £600k for loans with a term of over 5 years
Purpose:	New or additional borrowing only
Lending Product:	Term Loan
Lender Security:	Subject to the Lender's normal commercial criteria, all available security (business or personal, excluding PPR) should be considered to back the EFG loan
Premium Payment:	2% per annum, quarterly in advance against outstanding loan balance

Example of Type B lending (1)
The Application: • An existing business wishes to borrow £50k to refurbish its commercial premises. • It currently has a commercial mortgage of £400k on a property valued at £575k, representing LTV of 70%*, which is the Lender's maximum LTV. • It is anticipated that the refurbishment will add £50k of value to the property. • No more security is available. **Note: the 70% LTV is for illustrative purposes only – normal Lender credit criteria, including specification of LTVs, will apply in all instances.*
The Outcome : • The RM assesses that the Applicant can afford to repay £50k over a 3-year period, assessed according to the Lender's normal lending criteria. • The RM is minded, however, to decline the application because a) total facilities relating to the property will be £450k, against a revised property valuation of £625k, giving a LTV of 72%, which is above the Lender's maximum LTV; and b) there is no further security available. • The use of EFG to facilitate the additional funding requirement is, therefore, appropriate because the only issue preventing the approval of • the Application is the shortfall in the value of the security.
Example of Type B lending (2) • The Application is the same as in Example (1) above; however, the Borrower is offering to provide a Personal Guarantee for £25,000 supported by a charge over his main residential property. EFG is INELIGIBLE in these circumstances.
Example of Type B lending (3) • The Application is the same as in Example (1) above; however, the Borrower is offering an Unsupported Personal Guarantee. EFG is ELIGIBLE for the full additional borrowing requirement, Personal Guarantee also to be provided.

Flexibility between Type A and Type B facilities

In many Type B scenarios, following normal lending criteria, the availability of the additional security by the Borrower could in itself be sufficient to induce a Lender to provide a standard commercial facility for a proportion of the borrowing requirement.

A Type A EFG facility may then be available to make up any shortfall in the required amount. Taking the same situation as Example (1) above:

The Outcome – Using a commercial loan plus a Type A EFG instead of 100% Type B EFG:

- Following normal commercial lending criteria, the RM is prepared to lend without EFG backing so long as the LTV is no more than the bank's maximum LTV of 70%.

- The refurbishment creates additional security of £50k. At its maximum LTV of 70%, the bank is prepared to lend £35k on normal terms.

- As the Applicant requires a total of £50k there is still a £15k shortfall. The RM has assessed the Applicant's proposal as viable under normal lending criteria, and £15k is lent as a Type A EFG with the other £35k funded via a commercial loan.

Deciding whether to lend as Type A or Type B EFG

Where the option is available, the decision whether to lend solely as Type B EFG, or to split the lending as a combination of a secured commercial loan plus a Type A EFG-backed loan, is a commercial decision for each Lender.

3.5 Type E – Revolving Credit Guarantee

Overview

Type E EFG is used for new or additional borrowings via any of the eligible debt instruments detailed below, where the Borrower is viable and has no or only partial additional security to offer to the Lender (which is insufficient security to secure the borrowing requirement according to the Lender's normal credit criteria).

Type E EFG cannot to be used to replace or refinance existing Lender facilities, this is possible using the designate refinance option (Type G).

Where a Lender uses Type E EFG to support the provision of an increased limit on an existing eligible product, the Guarantee covers the specified EFG facility only and does NOT extend to the existing Lender facility or any excess position above the agreed limit.

The Lender can charge a margin and fee on the EFG facility in-line with normal commercial terms. This may include charging split margins on the EFG-backed element of the facility compared to the commercial facility if deemed appropriate by the Lender.

Eligibility Criteria

Guarantee Term:	Minimum 3 months up to a maximum 3 years. A Type E facility may be made available to a Borrower over a maximum initial period of 36 months from the granting of the facility. The extent to which the total possible term is utilised and the structure within that utilisation (e.g. 3 x 12 month facilities, 6 x 6 month facilities, 12 x 3 month facilities) is for the Lender to determine subject to their normal credit sanction and overdraft review procedures. If at any point during the Lender's normal cycle of reviews the facility, or support of the facility using EFG, is no longer required the Lender must mark the EFG facility as repaid on the Web Portal.
Minimum Amount:	£1k
Maximum Amount:	£1.2m
Purpose:	New or additional borrowing only

Lending Products:	Overdrafts Fixed Term Revolving Credit Facilities Business Credit (or Charge) Cards Bonds and Guarantees (Performance Bonds, VAT Deferment etc.) BACS facilities Stocking Finance Import Finance (Letters of Credit, Import Loans etc.) Merchant Services Multi-option Facilities (setting a limit which can be used across a variety of the above).
Lender Security:	Subject to the Lender's normal commercial criteria, all available security (business or personal, excluding PPR) should be considered to back the EFG facility.
Premium Payment:	Quarterly in advance against the additional 'top-up' element of the facility, irrespective of utilisation.
Facility Renewal Option:	At the end of the facility term, the Lender may determine whether or not the Borrower requires a further facility, and if so, whether EFG is necessary to enable that facility to be provided. If further use of EFG is deemed necessary then the Lender should process a new application in the usual way.
Default Procedure:	In the event of Borrower default, the Lender should realise all available security and apply these proceeds in direct reduction of a) outstanding Lender debt b) outstanding EFG-backed debt c) any excess position above the agreed facility limit.
Claim Against Guarantee:	Lender is entitled to claim 75% of the outstanding facility balance, up to a maximum of the EFG facility amount (subject to the Claim Limit). In addition, any interest that has accrued prior to the earlier of the date on which the Lender makes Demand for repayment on the Borrower and the scheduled expiry date of the facility may be included in the Claim on the Guarantee. The Guarantee does not extend to any excess position above the agreed EFG facility.

Operational Considerations

- Where the Lender has declined a Borrower's request for a new or increased overdraft facility or cancelled/reduced a facility in the preceding three months then use of EFG is not necessarily prohibited. However, the Lender should document the change in stance towards the Borrower and be prepared to justify it as necessary during an EFG audit.

- The Lender may act in accordance with their normal commercial practice with respect to managing limits, but must provide a clear explanation of the rationale for any decisions to meet Scheme audit requirements. In the event that the overall limit is reduced during the lifetime of the facility, the EFG facility should be reduced before any commercial element of the facility.

- There is no requirement for the Lender to specifically monitor receipt of funds credited to the overdraft current account during the normal course of business. Any pre-existing commercial overdraft facility is prior debt and ranks in priority to the EFG-backed 'top-up' facility, such that "business as usual" credits extinguish commercial exposure first.

<table>
<tr><td>Example of Type E lending</td></tr>
<tr><td>The Application:

The Borrower has an existing overdraft facility of £50k which is secured by a debenture over the assets of the business.
The company needs a £25k increase in its overdraft facility to fund the costs involved in bidding for a new contract – this contract has been granted to the company but is not due to come on stream for another 2 months.
The increase in the overdraft is required for a 6 month period only. The company has no additional security to provide (and the Directors have no personal wealth).
The company can afford to service the cost of the increased overdraft and repayment of the additional £25k will come from profitability linked to the new contract.
</td></tr>
<tr><td>The Outcome:

The Applicant would be eligible for an Type E EFG facility to 'top-up' their overdraft.
The total overdraft facility would be £75k, of which £50k would be the Lender overdraft facility and the remaining £25k would be backed by EFG.
</td></tr>
</table>

Type E EFG - Frequently Asked Questions

Can Type E EFG be used for a group overdraft facility?

Yes – Provided the group's turnover is below £41m and the other eligibility criteria are all met. In this case it is the group which is the Borrower.

Why is Type E EFG available for up to 36 months when most Lenders' normal maximum overdraft term is 12 months?

Although it is recognised that overdrafts are repayable on demand and usually subject to an annual renewal, the 36 month maximum enables the Lender to plan ahead, anticipating possible requests from Borrowers for renewal of the Type E EFG facility in parallel with their core overdraft facility, and ensures that the Lender has certainty that the guarantee remains in place in the event that, for example, circumstances mean that a planned review at 12 months is delayed for a quarter.

If at any point during the Lender's normal cycle of reviews the facility, or support of the facility using EFG, is no longer required the Lender must mark the EFG facility as repaid on the Web Portal.

Why is the minimum term 3 months?

This is for 3 reasons:

a) to correlate with the minimum term currently offered for an EFG term loan;
b) the administration involved in setting up an EFG facility would make shorter term facilities (1 or 2 months) potentially unattractive to operate and administer; and
c) the minimum Premium able to be collected for the EFG guarantee is for a 3-month period.

A customer's existing overdraft facility has 7 months until expiry. Can the Type E EFG facility be provided for the same period so that both facilities expire simultaneously?

Yes – A Type E EFG facility to support an overdraft can be provided for any term between 3 and 36 months, so a 7-month facility can be provided. Borrowers need to be made aware, however, that the guarantee Premiums will be collected quarterly in advance, with the first Premium collected within one month of draw down, and will not be reimbursed in the eventuality that the facility is not made available for the full duration of the relevant quarter. Therefore, for a 7-month facility, three Premiums would be collected, in months 1, 4 and 7, with the third Premium collected in month 7 being for quarter three (months 7 – 9) even though the facility will only be available for one month of that quarter.

What happens at expiry of the Type E EFG facility?

At expiry of the stated term of the Type E EFG facility, one of four things may occur:

- The outstanding balance on the Type E EFG facility is repaid by the Borrower and the limit cancelled; or
- The Lender could provide a new Type E EFG facility. The Lender must complete a new EFG application to confirm that use of EFG remains necessary and appropriate and that the eligibility criteria are satisfied; or
- The Lender could provide a commercial facility to replace the EFG facility, where EFG is no longer required or the Borrower no longer meets the criteria for EFG; or
- The Lender could, subject to eligibility criteria being satisfied, refinance the Type E EFG facility on to a term loan using either Type C or Type D EFG (whichever is applicable).

What happens if a Type E EFG facility reaches its expiry date and has not been renewed or repaid?

The EFG facility will cease to be guaranteed and all exposure risk will lie with the Lender.

The EFG Premium on a term loan is payable on the outstanding balance. For Type E EFG, why is the Premium paid on the limit of the EFG-backed facility (rather than the outstanding balance)? How is the Premium calculated?

The Premium is paid on the limit of the EFG facility, this is for three primary reasons:

a) to encourage the setting of appropriate Limits which accurately reflect the borrowing requirements of the business;
b) as it is consistent with Lenders' charging structures within which an arrangement fee is payable based on the value of the facility requested, irrespective of future utilisation; and
c) because, in the event of default, it is likely that the guaranteed overdraft will have been substantially fully used as the SME has access to the full facility.

If a Type E EFG facility is provided and, then, subsequently repaid by the Borrower (so that the full 36 month availability period is not fully utilised), is the Lender able to offer a subsequent EFG Overdraft Guarantee Facility at a later date?

Yes. Lenders have the ability for repeat use of Type E EFG. The limiting factor on the number, value and frequency of all EFG facilities which Lenders area able to provide to an SME if the *de minimis* State Aid limit.

If a Type E EFG facility is repaid in full, any subsequent request to provide another Type E facility will need to be processed as a new application.

Must a Type E EFG-backed overdraft be operated on a separate current account to the existing customer overdraft or must both be operated on the same account?

This is a commercial decision for the Lender. Ideally, the Type E EFG overdraft facility should be operated via a limit marked on the Borrower's main current account. Where an existing overdraft facility is already in place, the Type E EFG facility should be shown as an increased limit (over and above the existing overdraft limit) on the Borrower's main current account.

By operating a single current account, the Borrower needs to use only one cheque book and only has to manage one single account.

If the Type E EFG overdraft facility was to be operated via a separate current account to the Borrower's main current account, a number of potential issues would arise:

1) the Borrower would need to operate via 2 separate cheque books and 2 separate bank accounts thereby making cash management more difficult;
2) the Borrower could use one overdraft facility more than the other (for example, use the EFG-backed overdraft facility in full, whilst not using the "normal" overdraft which would be against the whole spirit of needing the EFG guarantee);
3) having 2 separate accounts may increase the likelihood of "cross firing" between the two accounts.

If a Lender's systems require two separate accounts to be operated, then the Lender will be required to demonstrate at audit that sufficient cross checks are in place to guard against preferential use of the EFG-backed facility over the normal (commercial) facility.

Where an Type E EFG facility has been provided for (say) 6 months, how can this facility be renewed for a further 6 months?

Provided that the Lender has originally requested the Type E EFG facility for a term of sufficient length to cover the initial and renewed periods, the renewal has been sanctioned according to the Lender's normal commercial procedures and arrangements for collection of the EFG Premium are in place, then the Lender has the necessary cover to provide a facility letter to the Borrower without further intervention.

If the EFG facility term has expired, subject to a full reassessment of the Borrower's need and eligibility for EFG, the Lender can complete a new Type E EFG application.

What happens if a Borrower exceeds the Type E EFG facility limit?

The Government guarantee covers the stated Type E EFG facility only and does not cover any excess position on an account or any element of the Borrower's "normal" overdraft facility. In the event of an excess occurring on the account, all liability for the excess balance lies therefore with the Lender.

Is the Type E EFG guaranteeing an overdraft affected at all by "Clayton's Case"?

The implications of Clayton's Case are fully covered in the EFG Legal Agreement. Operationally, the EFG guarantee operates according to the terms detailed in this Manual.

Do Lenders have to charge the same margin on a Type E EFG-backed overdraft as on the "normal" overdraft facility?

Normal commercial terms of the Lender apply.

Can normal excess fees be charged in the event of the Borrower exceeding the facility limit?

Normal commercial terms of the Lender apply.

A Lender's current facility documentation states that the customer overdraft is repayable upon Demand? Is this in any way affected by provision of an EFG Overdraft Guarantee Facility?

Normal legal terms of the Lender apply.

Can Lenders utilise capacity in a Type E EFG facility to reduce non-EFG exposure?

We would expect the overdraft (or other permitted revolving credit facility) to be operated within its normal commercial terms. We would **not** expect in the period leading up to default, or at the point of default, any headroom in the facility being utilised to reduce commercial exposure on other (non-EFG) facilities. This represents a transfer of risk and is not within the spirit of the scheme. This does not apply to a contracted loan repayment being presented for payment.

Does a Lender's existing facility documentation need to be amended in any way to accommodate use of Type E EFG?

The Lender's standard facility letter will require an additional paragraph covering EFG exposure (as with EFG term loans). Full details are provided in the EFG Legal Agreement.

What happens if EFG does not continue beyond 31 March 2015?

In the event that EFG were to be closed, under the existing provisions, the guarantee remains in place for the originally agreed duration on all facilities put in place prior to that date.

An additional provision has been introduced such that in the event of notification of closure of the scheme, the Lender is entitled to reassess the status of each Type E facility so that, if necessary, a replacement term loan EFG facility may be provided prior to the closure of the scheme.

3.6 Type F – Invoice Finance Guarantee

Overview

Type F EFG is intended as a flexible instrument to sit alongside a new or existing recourse invoice discounting or factoring facility.

Lenders make an assessment of the funding request, adopting their normal commercial lending criteria and document their decision in accordance with normal policy.

Where the level of funding which can be made available is below the amount required by client, the Lender may consider using Type F EFG to support an increased prepayment percentage/facility limit.

The Guarantee covers the specified EFG facility only and does NOT extend to the existing Lender facility or any overpaid position above the agreed limit.

Type F EFG cannot be used to replace or refinance existing Lender facilities, this is possible using the designated refinance option (Type H).

Eligibility Criteria

Guarantee Term:	Minimum 3 months up to a maximum of 3 years
Minimum Amount:	£1k
Maximum Amount:	£1.2m
Purpose:	New or additional borrowing only
Lending Product:	Invoice discounting or factoring.
Maximum Prepayment %:	Up to 30% of gross debtors (subject to total invoice finance facility percentage - Lender's existing line and additional EFG-backed element not exceeding 100% of gross debtors). The EFG guarantee facility must be defined with both a maximum value (in £) and an additional prepayment percentage.
Lender Security:	Subject to the Lender's normal commercial criteria. Assignment of debtor book may be complemented with the taking of additional security (business or

	personal, excluding PPR) if this forms part of the Lender's normal security policy.
Premium Payment:	2% annually payable quarterly in advance by the Borrower on the agreed level of Industry Average Utilisation Rate ("IAUR") applied to the Borrower's Type F EFG facility limit. The IAUR is to be informed by a defined ratio within the ABFA quarterly statistics, rounded up to the next multiple of 5 and then adding 10%.
Facility Renewal Option:	At the end of the facility term, the Lender may determine whether or not the Borrower requires a further EFG-backed facility, and if so, whether EFG is necessary to enable that facility to be provided. If further use of EFG is deemed necessary then the lender should process a new application in the usual way.
Default Procedure:	In event of Borrower default, the Lender should realise all available security and apply these proceeds in direct reduction of a) outstanding Lender debt b) outstanding EFG-backed debt c) any overpaid position above the agreed facility limit.
Claim Against Guarantee:	Lender is entitled to claim 75% of the outstanding balance of the utilised EFG-backed element (subject to the Claim Limit). In addition, any interest that has accrued prior to the earlier of the date on which the Lender makes Demand for repayment on the Borrower and the scheduled expiry date of the facility may be included in the Claim on the Guarantee. The Guarantee does not extend to any overpaid position above the agreed EFG facility.
Annual Portfolio Value	Annual additional EFG limits (total facility must be split EFG and non-EFG) multiplied by the prevailing IAUR.

Annual Claim Limit	Based on the Annual Portfolio Value originated in the period. Claim limit to be tabulated as follows: First £100k of Annual Portfolio Value 100% maximum gross default rate x Guarantee Rate of 75% = 75% Net Claim limit of first £100k of lending. Thereafter: Annual Portfolio value in excess of £100k for each Lender x 20% maximum gross default rate x Guarantee Rate of 75% = 15% net claim limit.

Operational Considerations:

- Neither the agreed funding limit nor the prepayment percentage provided by the Lender on any existing facilities may be reduced except in accordance with the Lender's normal commercial criteria for managing those facilities.
- In the event a funding limit is reduced during the lifetime of the facility, the EFG facility should be reduced before any commercial element of the facility.

Example of Type F lending
Assume a client has gross debtors of £1m with an agreed prepayment percentage or initial prepayment of 80%. Subject to the Borrower and proposition meeting EFG eligibility criteria, the Lender could agree to increase the prepayment percentage by 20% (100% - 80%) with an upper limit of a maximum of £200k. For EFG purposes this will be treated as a maximum potential exposure of £200k and recorded as such in all facility documentation. However, at any one time, the actual liability of 20% of gross debtors could be lower than this value. It is anticipated that the Lender will use its **facility limit** (on internal systems) to control the maximum guarantee liability internally. The Borrower will be charged the EFG guarantee Premium on £200k multiplied by the IAUR. In the event of Borrower default, the Lender will collect the book debts and realise any other available security. These funds would then be used to repay the outstanding balance on the funding line.

In the event of there being any shortfall in repaying the outstanding indebtedness, a claim can be made under the EFG guarantee facility subject **to the lower of the upper EFG facility limit or the value of 20% of gross debtors** at the time of the event of default. The Claim will be settled for 75% of the eligible outstanding debt.

In the event of the Lender requiring an increase in the upper limit of the guaranteed facility (say due to the growth of the business) then a new EFG application for the additional amount would need to be made and the two facilities operated concurrently, but with the older facility being fully utilised before use is made of the newer one.

Frequently Asked Questions:

Why is the Type F EFG Invoice Finance Guarantee Facility available for a maximum of three years only? What happens when the three years have passed?

A three-year timeframe has been deemed a suitable maximum period to offer working capital assistance to SMEs before undertaking a re-assessment of the Borrower's need and eligibility for support from the EFG scheme.

A facility renewal option has been introduced so that, subject to a full reassessment of EFG eligibility and there being a continued funding gap between the level of funding the Lender is able to provide on a commercial basis (assessed according to the Lenders normal commercial policy) a new Type F EFG facility may be provided, including for the purpose of specifically 'managing down' the previous EFG-back exposure.

The limiting factor on the number, value and frequency of all EFG facilities which Lender are able to provide to an SME is the *de minimis* State Aid Limit.

What happens if the guarantee facility reaches expiry and has not been renewed (up to a maximum period of 3 years) or repaid?

The guarantee would expire and all exposure and risk would lie with the Lender.

Does the additional prepayment percentage have to be expressed as a proportion of gross debtors as this measure is not to calculate available funding?

In considering the additional prepayment percentage, the Scheme links this to gross debtors as this provides Lenders with the broadest possible measure of debtors on which to make their assessment.

This <u>does not prevent</u> Lenders from deducting certain debtors from the gross figure to arrive at a level of 'eligible debtors' on which to base their funding tabulation, in line with their normal commercial practice. Lenders should adopt the measure using in their normal course of business when stating the additional prepayment percentage.

Is the EFG available to factoring companies as well as invoice discounters?

Yes, subject to accreditation, it is open to all Lenders operating in the invoice finance sector which lend to eligible SMEs on a recourse basis.

What will be the audit process for invoice financiers?

BBB have appointed auditors familiar with the invoice finance sector to review a sample of facilities granted by each Lender.

What level of due diligence should we undertake when assessing Invoice Finance facilities?

Lenders should make an assessment of the funding required, adopting their normal commercial lending criteria (being no more or less rigorous than usual) and document their decision in accordance with their normal policy.

Where the level of funding which can be made available is below the amount required by the SME, the Lender may consider using Type F EFG to support a higher prepayment level/facility limit for the additional requirement.

The Lender is to confirm that security has been investigated in accordance with the Lender's normal commercial policy. So Lenders will not therefore need to deviate from their current security process by extending investigations to areas not currently reviewed or by taking security types outside of those already adopted by the Lender.

Where an IF provider operates under "guidelines" rather than policies with discretion exercised by credit on a case-by-case basis then, for EFG audit trail purposes, it is important that there is sufficient information on file to confirm that the use of EFG is compatible with those guidelines.

How is the premium calculated on Invoice Finance facilities?

The premium will be 2% per annum, payable quarterly on the agreed level of 'industry average utilisation rate' ("IAUR") applied to the Type F EFG limits.

The IAUR used within the calculation is to be informed by ABFA quarterly statistics, referencing 'Total Facilities Agreed' rounded up to the next multiple of five; plus an additional margin of 10%.

The IAUR applied is to be reviewed annually against ABFA Quarterly Statistics for the quarter ending 31 December, with any change implemented with effect from 1 April (to tie in the scheme's financial year).

The IAUR applied to each individual Type F EFG facility will be the figure in operation when the facility is originated, which will apply for the full term of the guaranteed facility.

ABFA member data are collected and analysed, and statistics are independently prepared, by the research unit of the Finance and Leasing Association (FLA).

The IAUR applied for premium calculation will only be adjusted at the annual review if utilisation rates, as evidenced by ABFA statistics, have moved by at least +/- 5% since the previous review.

In the event that there is an in-year movement of the ratio of 'Total Advances' to 'Total Facilities Agreed' by +/-10% or greater the BBB may adjust the IAUR in-year.

Example: Type F EFG facility has a headline value of £1m
IAUR is (say) 60%
Premium Rate is 2.0%

Therefore the Annual Premium due is £1m x 60% x2.0%
= £12,000, or £3,000 per quarter.

Can EFG be used to support the continuation of existing Invoice Finance facilities?

If application of the Lenders normal commercial policy would result in a limit otherwise being reduced the Lender may transfer the element of the facility which is no longer a commercial risk to EFG using the designated refinance option (Type H). For example if the Lender's policy would result in the prepayment level being reduced from 85% to 75%, subject to satisfaction of the eligibility criteria an Type F EFG facility could be provided for a 10% top-up on prepayment returning the total prepayment level back to 85%).

How can EFG support a growing business using Invoice Finance?

It is accepted that this facility does not enable the absolute upper limit for an EFG backed facility to grow with the business, however, if a higher absolute limit is required, Lenders may increase the EFG facility following their normal procedure.

What happens if EFG does not continue beyond 31 March 2015?

In the event that EFG were to be closed, under the existing provisions, the guarantee remains in place for the originally agreed duration on all facilities put in place prior to that date. An additional provision has been introduced such that in the event of notification of closure of the scheme, the Lender is entitled to reassess the status of each Type F facility plus the respective refinance variant Type H so that, if necessary, a replacement EFG facility of whatever Type is considered most appropriate to the requirements of the Borrower may be provided prior to the closure of the scheme.

Are there any specific financial ratio tests which must be undertaken when considering EFG eligibility?

There are no specific financial tests (minimum Net Worth etc.) which must be performed as part of the Lender's assessment of an SME's eligibility for support under EFG.

However, Lenders are be required to confirm on the Web Portal that EFG is not used with 'businesses in difficulty' (see Section 2.3)

3.7 Type C – New Term Loan for Overdraft Refinancing

Overview

A Type C EFG term loan is aimed at existing businesses which:

- Have built-up "hardcore" positions on their current overdraft facility;
- May require additional headroom on their overdraft facility to enable continued trading; and
- Have no or only partial additional security to offer to the Lender. (Where additional security is being provided by the Borrower as part of the EFG proposal, the application should be still be entered on to the EFG Web Portal as a Type C loan.)

Type C is designed to help put the business on a more stable financial footing and to improve the Applicant's working capital position. In all instances, the business must be able to service its overall borrowing requirement. Where hardcore debt has developed due to trading losses, the Lender must apply normal lending criteria in assessing the business' likelihood of returning to profitability and being able to service future borrowing requirements.

When providing a Type C EFG facility, the decision on what proportion of the Applicant's overdraft is transferred to term loan is the responsibility of the Lender, to be made in accordance with the Lender's normal commercial practices.

Where the refinancing is for all of the existing overdraft facility, the Lender must assess whether the Applicant has an ongoing requirement for an overdraft, in accordance with their normal commercial practice. Type E EFG may be used to support the provision of an overdraft where a facility is required but the business has insufficient security to allow the Lender to provide a facility on a commercial basis.

There is no requirement on the Lender to increase the overall level of funding when using Type C EFG, or make an overdraft facility available following the refinancing if the business does not require a facility. A straight swap of hardcore debt from overdraft to EFG term loan without the provision of a continued overdraft facility is ELIGIBLE if this is the appropriate strategy and funding structure for the business.

For clarity, where part of a new EFG term loan is used to repay a portion of an overdraft with no wider debt consolidation this is Type C refinancing, even when the primary motive is additional funding and an overdraft repayment is incidental to a term loan for investment.

Eligibility Criteria

Guarantee Term:	Minimum 3 months up to maximum 10 years
Minimum Amount:	£1k
Maximum Amount:	£1.2m for loans with a term of up to 5 years £600k for loans with a term of over 5 years
Purpose:	Predominantly the refinance of overdraft hardcore to term loan, although may include the provision of additional funding.
Lending Product:	Term Loan
Lender Security:	Subject to the Lender's normal commercial criteria, all available security (business or personal, excluding PPR) should be considered to back the EFG loan
Premium Payment:	2% per annum, quarterly in advance against outstanding loan balance

Portfolio Restrictions:

Type C is one of the four permitted Refinancing Types under EFG. Collectively use of these Types is limited to a maximum of 20% of each Lender's utilised EFG Lending Allocation at any point in time. The relevance of this 20% cap will be reviewed periodically by BBB.

Example of Type C lending

The Application:
 	
• An existing business requires £50k of additional working capital to continue trading. The existing facilities are:
    ○ a commercial mortgage of £300k on a property valued at £575k
    ○ a hardcore overdraft of £100k
• Total existing debt of £400k represents 70%* LTV on the security of £575k. This is the bank's maximum LTV and no more security is available.

• The RM applies normal commercial lending criteria and believes that the business can afford to repay £100k over a 10-year period, assessed according to normal lending criteria. • As the facilities are already at the maximum LTV, and as there is no more security available, the RM is minded, however, to decline the application due to insufficient security. **Note: the 70% LTV is for illustrative purposes only – normal Lender credit criteria, including specification of LTVs, will apply in all instances.*

The Outcome:
 	
• The use of Type C EFG to refinance the overdraft and facilitate the additional funding requirement is appropriate because the only issue preventing the approval of the application is the lack of security.
• The resulting position is as follows:
  ○ a commercial mortgage of £300k on a property valued at £575k.
  ○ Type C EFG loan of £100k.
  ○ £50k fully fluctuating overdraft.

Frequently Asked Questions:

If the Applicant does not wish to have a replacement overdraft facility, can the existing overdraft still be transferred to an EFG loan?

Yes.

When all (or substantially all) of the overdraft facility is being refinanced, rather than provide a replacement overdraft, can alternative products such as invoice discounting or business visa facility be provided instead?

Yes – decision making on the structure of any facilities is devolved to the Lender, to be made in accordance with their normal commercial practices.

3.8 Type D – New Term Loan for Debt Consolidation or Refinancing

Overview

An EFG term loan aimed at businesses which have existing borrowing via term loan (or a term loan plus overdraft (or other permitted revolving facility) and / or invoice finance).

The business is viable but is no longer able (or is forecast to be unable) to meet the repayment obligations on its existing debt and a refinance of existing facilities onto a single term loan is desired, with an extended repayment term or capital repayment holiday **to ease cash flow pressure and ensure ongoing viability**. In addition, the value of existing security held by the Lender is inadequate to meet the Lender's normal security requirements and the Borrower has no more security available.

There is no requirement on the Lender to increase the overall level of funding when using Type D EFG, or continue any non-term facilities included in the debt consolidation.

Where an Applicant has a number of facilities and is struggling to meet the existing repayment terms, it is the Lender's decision as to which of the facilities are included within the rescheduling exercise.

Rather than guaranteeing the whole of the consolidated loan balance under EFG (which may be expensive for the Borrower), the Lender has the option of splitting the consolidated term loan into two separate loan facilities – one commercial facility secured by existing Lender security and one secured by the EFG guarantee. In this scenario the terms and conditions and repayment profiles of the two loans should be identical, the only exception being pricing – where the Lender may reflect the differing risk on each facility according to its normal lending practice.

This product is available to conventional EFG Lenders (providers of term loans and overdrafts etc.) and invoice financiers.

Lenders must not use Type D EFG to refinance existing debt when future viability is uncertain and where it appears likely that, even following the refinance, the Borrower may soon enter administration or insolvency proceedings. Such a transaction would be viewed as a transfer of risk to the taxpayer and a potential misuse of the scheme.

Eligibility Criteria

Guarantee Term:	Minimum 3 months up to maximum 10 years
Minimum Amount:	£1k
Maximum Amount:	£1.2m for loans with a term of up to 5 years £600k for loans with a term of over 5 years
Purpose:	Predominantly refinance of existing lending, however an increase in exposure (beyond the sum of the current outstanding value(s) of the facility(ies) being consolidated and rescheduled) is permitted.
Lending Product:	Term Loan
Lender Security:	Subject to the Lender's normal commercial criteria, all available security (business or personal, excluding PPR) should be considered to back the EFG Loan
Premium Payment:	2% per annum, quarterly in advance against outstanding loan balance

Portfolio Restrictions:

Type D is one of the four permitted refinance Types under EFG, collectively usage of these Types is limited to a maximum of 20% of each Lender's utilised EFG Lending Allocation at any point in time. This 20% cap will be reviewed periodically by BBB.

Notes for Invoice Financiers:

Where a current invoice finance facility becomes overpaid for a valid commercial reason (for example, due to a customer or debtor insolvency or a withdrawal of a credit limit), then an EFG term loan facility (Type D) could be considered to repay the overpaid position, enabling a phased repayment of the overpaid position to avoid undue cash flow strain, where existing security value (where there is security) is insufficient to meet normal Lender requirements and no further security is available.

Neither the agreed funding limit nor the prepayment percentage provided by the Lender on any existing facilities may be reduced except in accordance with the Lender's normal commercial criteria for managing those facilities. Transfer of risk from the Lender to the Government on existing borrowings by retrospectively reducing an existing prepayment percentage or limit in order to create opportunity for refinance by EFG-backed lending is outside the spirit of the programme. For the avoidance of doubt, this does not affect day-to-day changes in the outstanding balance as invoices are presented or paid.

Example of Type D lending (1) – Existing facility is single term loan, <u>secured</u>
The Application: • An existing business has a £95k term loan backed by £135k of security (70% LTV). • Six months later the term loan outstanding is £90k and security value has fallen to £90k (100% LTV). No more security is available. • The Borrower is struggling to meet the monthly capital and interest repayments on the loan and appears likely to default on the loan unless the term of the existing loan is extended or switched to interest-only. • The RM applies normal commercial lending criteria and believes that the business can service reduced monthly repayment costs (as a consequence of extending the loan term). • However, as the LTV ratio is now considerably beyond the maximum of 70%*, and as there is no more security available, the RM is aware that a sanction of restructured facilities is unlikely due to a lack of security cover. • By using EFG Type D, the restructure is possible. **Note: the 70% LTV is for illustrative purposes only – normal Lender credit criteria, including specification of LTVs, will apply in all instances.*
The Outcome: • The Lender will split the existing £90k term loan into two loans: 1. Loan X (commercial risk) would be for £63k (providing 70% LTV against current security value of £90k). 2. Loan Y (non-commercial risk) for £27k to be supported by an EFG guarantee.

Example of Type D lending (2) – Existing facility is single term loan, <u>unsecured</u>
The Application: • An existing business has an unsecured £95k term loan. • Six months later the term loan outstanding is £90k. • The Borrower is struggling to meet the monthly capital and interest repayments on the loan and appears likely to default on the loan unless the term of the existing loan is extended or switched to interest-only. • The RM applies normal commercial lending criteria and believes that the business, after extending the outstanding loan term, could service the reduced monthly repayment cost. • However, as there is no security for the debt, and as none is available, the RM is minded to call in the loan rather than restructure, because there is insufficient security.
The Outcome: • By using EFG Type D, the restructure is possible. • The £90k term loan is refinanced as a £90k Type D loan, supported by a 75% EFG guarantee.

Example of Type D lending (3) – Multiple term loans, secured

The Application:

- An existing business has £210k of debt backed by security valued at £300k (LTV of 70%*), as follows:

	Debt (£000)	Security (£000)	LTV (%)
Term loan 1	60	80	75%
Term loan 2	100	120	83%
Term loan 3	50	100	50%
	210	300	70%*

**Note: the 70% LTV is for illustrative purposes only – normal Lender credit criteria, including specification of LTVs, will apply in all instances.*

- Six months later there is £170k of debt backed by security valued at £210k (LTV of 81%) as follows:

	Debt (£000)	Security (£000)	LTV (%)
Term loan 1	50	55	91%
Term loan 2	90	85	106%
Term loan 3	30	70	43%
	170	210	81%

- The Borrower is struggling to meet the monthly capital and interest repayments on the loans and appears likely to default on the loans unless the term of the existing debt is restructured.
- The Lender wishes to extend the outstanding term on Loans 2 and 3 to reduce monthly cost to the Borrower.
- However, as the facilities are now considerably beyond the maximum LTV of 70%, and as there is no more security available, the RM is therefore minded to call in the loan rather than restructure, because there is insufficient security.

The Outcome:

- Where a Type D EFG is used to refinance multiple loans, and where there is some security available, the Lender will have the option of:

a) refinancing the entire debt as partially secured EFG debt;
b) splitting the debt into secured non-EFG debt plus unsecured EFG debt; or,
c) splitting the debt into secured non-EFG debt plus partially secured EFG debt.

- In this instance the Lender has chosen option “b” – keeping Term Loan 1 as non-EFG debt and refinancing Term Loans 2 and 3 as EFG backed and non-EFG backed loans in proportion to the available security – as follows:
- The RM calculates the additional security required to achieve maximum LTV on Term Loan 1:
  - £50k / 70% = £71.4k
- The RM then calculates how much remaining security is available to cover Term Loans 2 and 3:
  - £210k - £71.4k = £138.6k
- The RM then calculates how much non-EFG debt (Loan X) will be available using this security:
  - £138.6k x 70% = £97k
- A Type D EFG is used to secure the remaining balance (Loan Y)
  - £170k - £50k - £97k = £23k

Example of Type D lending (4) – Multiple loans plus overdraft facility, <u>secured</u>

The Application:

- An existing business has £220k of debt backed by a package of security valued at £272k (overall LTV of 81%), as follows:

Existing Facilities	**Existing Security Value**
Overdraft – £50k limit (£30k hardcore debt)	Debenture – £132k
Term Loan 1 – £50k	Legal Charge 1 – £55k
Term Loan 2 – £90k	Legal Charge 2 – £85k
Term Loan 3 – £30k	
Total Debt – £220k	**Total Security – £272k**

- The Lender may refinance the full £220k of existing exposure or any proportion of it as the Lender deems appropriate.
- There is no requirement for a Lender to ensure that an overdraft facility is still in place following the refinance, although this may be appropriate.
- In this example, it is assumed that the full £220k exposure will be refinanced (including the £50k overdraft facility rather than just the hardcore element) and that a replacement overdraft of £25k will be provided.
- In order to calculate the appropriate levels of Loans X (commercial risk) and Y (non-commercial risk) for the above example, the following process may apply:
    - The Lender should value existing security (according to normal Lender security valuation methodology) and deduct from this security value a suitable level of cover for the facilities not included within the refinance exercise – in this example, the replacement overdraft facility of £25k.
    - From the remaining security available, the Lender should then calculate how much can be allocated to the "secured" Loan X (*Note: 70% LTV is for illustrative purposes only – normal Lender credit criteria, including specification of LTVs, will apply in all instances*.)
    - The remaining balance should be allocated to Loan Y.

The Outcome:
 	
• Overdraft – £25k (replacement overdraft facility at level deemed appropriate by the Lender).
• Lender takes total available security of £272k and subtracts the necessary amount to provide security for the £25k replacement overdraft (£25k, requiring 70% LTV, gives a total security requirement of £35k). Remaining security available is £272k - £35k = £237k.
• From the £237k of remaining security, the Lender needs to calculate the maximum level of term debt this can secure at normal LTV ratios.
• So, £237k at 70% LTV would secure a maximum loan of £166k. Loan X would, therefore, be £166k.
• The remaining term loan exposure constitutes the balance on Loan Y (£220k - £166k = £54k).
• Total facilities are:
  o Replacement overdraft – £25k
  o Term Loan X (commercial risk) – £166k
  o Term Loan Y (non-commercial risk, EFG-backed) – £54k

Example for Invoice Financiers
A debtor of your client has recently had its credit rating reduced from "medium risk" to "high risk" and consequently, you reduce your prepayment percentage for this debtor from 80% to 65%. As a consequence, you have an immediate overpaid position on this debtor of £100k. Rather than claw this amount back in one lump sum by paying less than 65% on subsequent invoices raised with this debtor, you agree instead to refinance this £100k overpayment onto an EFG term loan, repayable over 12 months with monthly repayments. In order to be eligible for an EFG loan, you credit assess your client to satisfy yourself that the £100k can be repaid from on-going cash flow over the next 12 months and also satisfy yourself on whether the client has any additional security they can provide to secure the new term loan

Frequently Asked Questions:

Do the facilities being refinanced need to have been provided by the existing Lender, i.e. can a Lender refinance borrowings from other Lenders assuming the eligibility criteria for Type D are met?

When examining a "new to Lender" borrowing proposal, EFG can be considered if all eligibility criteria for EFG are met. However, in these circumstances, any EFG facility provided would by implication be classified as either a Type A or Type B loan, rather than a Type D refinanced loan.

Type D is for refinancing of term loans of existing customers only.

The Lender wishes to undertake a debt restructuring exercise whereby all existing term loans and the outstanding balance on overdraft are to be consolidated onto one new term loan. The Borrower has insufficient security to cover the existing level of debt but can afford repayments on a new term loan over an extended period of time. Can EFG be used to assist with this scenario?

On the basis the proposed new loan is serviceable, the Lender can confirm that the restructure must occur to ensure on-going viability of the Borrower and the Borrower has insufficient security, it appears that this scenario would be eligible for Type D under EFG. See worked example 4 above for an illustration of this type of scenario.

Some of the existing loans for a Borrower are already on a term of 15 years. Is there any way to include loans with an existing term of 10 years plus within the refinance option?

It is up to the Lender to choose which existing loans can be refinanced using this product – it is acknowledged that where the existing term loan is for more than 10 years, it may not be appropriate to include within the refinance scenario (as by switching to EFG, the term would be shorter and, therefore, cause additional strain on the cash flow of the Borrower). EFG is really aimed at short term loans (say 2-5 years) where the Borrower is struggling to meet existing repayments and where a lengthening of the term up to 10 years would ease that cash flow strain.

Can different margins be charged on Loans X and Y in example 4?

Yes – The margins to be charged are determined by the Lender according to their normal commercial practice.

Why do the terms of Loans X (commercial risk) and Y (EFG-backed) have to be the same (other than on pricing)?

BBB would not wish to see Loan X being repaid at an accelerated pace to Loan Y, thereby leaving the higher risk proportion of the debt (covered by the Government guarantee) outstanding for longer.

Can asset finance and HP loans be refinanced under Type D?

HP loans are outside the scope of Type D and, therefore, ineligible for EFG.

The Lender's standard facility documentation includes an all monies and liabilities clause whereby all security charged covers all indebtedness of the Borrower to the Lender. If existing term debt is restructured via an EFG refinance, the security charged for the old term loan must now be classed as existing collateral for the EFG term loan. If the Borrower subsequently goes into default, does this mean that the EFG loan has to be repaid before any other Lender indebtedness?

By refinancing an existing term loan(s) onto an EFG term loan, the Lender is gaining the benefit of a 75% guarantee from the Government to support an existing borrowing scenario (whereas a Government guarantee would normally only apply when <u>additional</u> debt is being provided to the Borrower). The Lender's potential loss position with this Borrower is, therefore, reduced due to the provision of the Government guarantee.

In the event of the Borrower subsequently defaulting, security relating to the refinanced term loan(s) would be realised and these proceeds would be used to repay the commercial non-EFG term debt in the first instance. However, as the Government has provided a supplementary guarantee to help refinance this same term debt, it is only right and proper that any security proceeds should then be used to pay down the outstanding balance on any remaining EFG exposure. A claim under the Government guarantee could then be made for the outstanding EFG exposure.

Where the Lender lists the same security items in facility letters for all Borrower exposure (for example, term loans, which are being refinanced but the same security is also listed for an overdraft, which is not part of the refinance), it is recognised that under a default scenario, the Lender is likely to repay the overdraft exposure first. This is allowed and a change from this practice is not required. The expansion of Type D does not alter the general principles relating to the realisation of security in connection with EFG lending as set out in Schedule 2 of the EFG Legal Agreement.

What happens where the existing security for term debt includes a Personal Guarantee supported by a charge over a PPR – does this also have to be listed as security for the EFG-backed loan?

This is the one exception to the existing security rule – where any form of charge over a PPR (direct or indirect) is included within the existing term loan security package, this must not be included as security for the Type D refinance loan.

When a debt consolidation exercise is undertaken, the Lender often wishes to marginally increase overall exposure on the consolidated term loan to cover fees or to provide a slight top up in exposure to the Borrower. Can the term loan exposure level be increased under Type D EFG refinance?

An increase in term loan exposure is allowed so long as the increase is included at the time of the refinance exercise and is made subject to all the standard EFG eligibility criteria.

Where existing term loans are due to expire and / or these have a lump sum repayment profile, is an EFG refinance allowed to extend the term of these loans?

Provided the core criteria for Type D are met – i.e. the Borrower is unable to continue to meet the existing loan repayments, a default will occur unless a rescheduling occurs and security is inadequate to meet normal Lender requirements – then this scenario should be eligible for EFG refinance.

Why is a Lender's utilisation for refinance EFG Types capped at 20%?

BIS is keen to ensure that refinance EFG Types are being correctly operated by Lenders and also that they are not being used as a vehicle for shifting riskier existing borrowings from the Lender's balance sheet onto the taxpayer. A limitation on each Lender's entitlement to utilise the refinance option will allow BIS to review utilisation. This cap may be reviewed periodically by BBB.

3.9 Type G – Revolving Credit Refinance Guarantee

Overview

If application of the Lenders normal commercial policy would result in an existing customer's limit otherwise being reduced on the basis of increased risk, such that existing security plus any additional security available is not sufficient to support provision of the facility, the Lender may consider transferring the element which is no longer a commercial risk to EFG using Type G EFG.

This will preserve the Borrower's access to finance, whilst retaining the existing debt instrument (which may be any product permitted under Type E EFG) and avoiding the additional cash burden of capital repayments which would result from transferring the debt to term loan (permitted under Type D EFG).

The decision on what proportion of the Lender's existing facility is transferred to EFG is the responsibility of the Lender, to be made in accordance with the Lender's normal commercial practices.

There is no requirement for the Lender to increase the overall level of funding when using Type G EFG. However, if the Lender choses to provide additional lending this is permitted.

The Guarantee covers the specified EFG facility only and does NOT extend to the commercial risk element of the facility or any excess position above the agreed limit.

The Lender can charge a margin and fee on the EFG facility in-line with normal commercial terms. This may include charging split margins on the EFG-backed element of the facility compared to the commercial facility if deemed appropriate by the Lender.

Eligibility Criteria

Guarantee Term:	Minimum 3 months up to a maximum 3 years. A Type G facility may be made available to a Borrower over a maximum initial period of 36 months from the granting of the facility. The extent to which the total possible term is utilised and the structure within that utilisation (e.g. 3 x 12 month facilities, 6 x 6 month facilities, 12 x 3 month facilities) is for the Lender to determine subject to their normal credit sanction and overdraft review procedures.

	If at any point during the Lender's normal cycle of reviews the facility, or support of the facility using EFG, is no longer required the Lender must mark the EFG facility as repaid on the Web Portal.
Minimum Amount:	£1k
Maximum Amount:	£1.2m
Purpose:	Existing borrowing plus any additional borrowing
Lending Products:	Overdrafts Fixed Term Revolving Credit Facilities Business Credit (or Charge) Cards Bonds and Guarantees (Performance Bonds, VAT Deferment etc.) BACS facilities Stocking Finance Import Finance (Letters of Credit, Import Loans etc.) Merchant Services Multi-option Facilities (setting a limit which can be used across a variety of the above).
Lender Security:	Subject to the Lender's normal commercial criteria, all available security (business or personal, excluding PPR) should be considered to back the EFG facility.
Premium Payment:	Quarterly in advance against the additional 'top-up' element of the facility, irrespective of utilisation.
Facility Renewal Option:	At the end of the facility term, the Lender may determine whether or not the Borrower requires a further facility, and if so, whether EFG is necessary to enable that facility to be provided. If further use of EFG is deemed necessary then the Lender should process a new application in the usual way.
Default Procedure:	In the event of Borrower default, the Lender should realise all available security and apply these proceeds in direct reduction of a) outstanding Lender debt b) outstanding EFG-backed debt c) any excess position above the agreed facility limit.

Claim Against Guarantee:	Lender is entitled to claim 75% of the outstanding facility balance, up to a maximum of the EFG facility amount (subject to the Claim Limit). In addition, any interest that has accrued prior to the earlier of the date on which the Lender makes Demand for repayment on the Borrower and the scheduled expiry date of the facility may be included in the Claim on the Guarantee. The Guarantee does not extend to any excess position above the agreed EFG facility.

Operational Considerations:

- The Lender may act in accordance with their normal commercial practice with respect to managing limits, but must provide a clear explanation of the rationale for any decisions to meet Scheme audit requirements. In the event a limit is reduced during the lifetime of the facility, the EFG facility should be reduced before any commercial element of the facility.

- There is no requirement for the Lender to monitor receipt of funds credited to the overdraft current account during the normal course of business. As prior debt any existing commercial overdraft facility rank in priority to the EFG-backed 'top-up' facility, such that business as usual credits extinguish commercial exposure first.

Portfolio Restrictions:

Type G is one of four permitted refinance Types under EFG, collectively usage of these Types is limited to a maximum 20% of each of the Lender's utilised EFG Lending Allocation at any point in time. This 20% cap will be reviewed periodically by BBB

Frequently Asked Questions:

Please see FAQ for Type E EFG.

3.10 Type H – Invoice Finance Refinance Guarantee

Overview

Lenders are currently able to transfer overpaid positions resulting from external shock (debtor insolvency, withdrawal of credit limit etc.) on invoice finance facilities onto a Type D EFG-backed loan but cannot deliver similar continued support through the invoice finance mechanism.

If application of the Lenders normal commercial policy, including considerations regarding the availability of security, would result in a facility limit or prepayment percentage otherwise being reduced the Lender may consider transferring the element of the facility which is no longer a commercial risk to EFG using Type H EFG.

This will preserve the Borrower's access to finance, whilst retaining the flexibility of the invoice finance product and avoiding the additional cash burden of capital repayments which would result from transferring the debt to term loan (permitted under Type D EFG), which may also not be a product offered by some specialist Lenders.

The decision on what proportion of the Lender's existing facility is transferred to EFG is the responsibility of the Lender, to be made in accordance with the Lender's normal commercial practices.

There is no requirement for the Lender to increase the overall level of funding when using Type G EFG. However, if the Lender choses to provide additional lending this is permitted.

The Guarantee covers the specified EFG facility only and does NOT extend to the commercial risk element of the facility or any overpaid position above the agreed limit.

Eligibility Criteria

Guarantee Term:	Minimum 3 months up to a maximum of 3 years
Minimum Amount:	£1k
Maximum Amount:	£1.2m
Purpose:	Existing borrowing plus any additional borrowing
Lending Product:	Invoice discounting or factoring.

Maximum Prepayment %:	Up to 30% of gross debtors (subject to total invoice finance facility percentage - Lender's existing line and additional EFG-backed element not exceeding 100% of gross debtors). The EFG guarantee facility must be defined with both a maximum value (in £) and an additional prepayment percentage.
Lender Security:	Subject to the Lender's normal commercial criteria. Assignment of debtor book may be complemented with the taking of additional security (business or personal, excluding PPR) if this forms part of the Lender's normal security policy.
Premium Payment:	2% annually payable quarterly in advance by the Borrower on the agreed level of Industry Average Utilisation Rate ("IAUR") applied to the Borrower's Type F EFG facility limit. The IAUR is to be informed by ABFA quarterly statistics, rounded up to the next multiple of 5 plus 10%.
Facility Renewal Option:	At the end of the facility term, the Lender may determine whether or not the Borrower requires a further EFG-backed facility, and if so, whether EFG is necessary to enable that facility to be provided. If further use of EFG is deemed necessary then the lender should process a new application in the usual way.
Default Procedure:	In event of Borrower default, the Lender should realise all available security and apply these proceeds in direct reduction of a) outstanding Lender debt b) outstanding EFG-backed debt c)any overpaid position above the agreed facility limit.
Claim Against Guarantee:	Lender is entitled to claim 75% of the outstanding balance of the utilised EFG-backed element (subject to the Claim Limit).

	In addition, any interest that has accrued prior to the earlier of the date on which the Lender makes Demand for repayment on the Borrower and the scheduled expiry date of the facility may be included in the Claim on the Guarantee. The Guarantee does not extend to any overpaid position above the agreed EFG facility.
Annual Portfolio Value	Annual additional EFG limits (total facility must be split EFG and non-EFG) multiplied by the prevailing IAUR.
Annual Claim Limit	Based on the Annual Portfolio Value originated in the period. Claim limit to be tabulated as follows: First £100k of Annual Portfolio Value 100% maximum gross default rate x Guarantee Rate of 75% = 75% Net Claim limit of first £x of lending. Thereafter: Annual Portfolio value in excess of £100k for each Lender x 20% maximum gross default rate x Guarantee Rate of 75% = 15% net claim limit.

Operational Considerations:

- Neither the agreed funding limit nor the prepayment percentage provided by the Lender on any existing facilities may be reduced except in accordance with the Lender's normal commercial criteria for managing those facilities.
- In the event a funding limit is reduced during the lifetime of the facility, the EFG facility should be reduced before any commercial element of the facility.

Eligibility Restrictions:

Type H is one of four permitted refinance Types under EFG, collectively usage of these Types is limited to a maximum 20% of each of the Lender's utilised EFG Lending Allocation at any point in time. This 20% cap will be reviewed periodically by BBB

Example:
Lender prepayment reduced from 85% to 75% with an EFG facility provided to replace the 10% reduction returning the total prepayment level to 85%.

Type H EFG - Frequently Asked Questions

Please see FAQ for Type F EFG.

4 EFG for CDFIs

4.1 Policy Summary

EFG may be used to allow banks to lend capital to CDFIs for subsequent on-lending to SMEs. This allows EFG to support the CDFI sector while also encouraging commercial relationships between banks and CDFIs.

This approach works in the same way as "conventional" EFG in most respects but with some changes as follows:

- It allows EFG lending for the purpose of providing capital for on-lending (which is otherwise ineligible).

- The CDFI is not required to pay the 2% per annum Premium on the money it borrows from a bank under an EFG facility. This is in recognition of the particular issues that CDFIs face in raising capital and the need to ensure that CDFI customers are able to access the finance they need.

- It operates the EFG Claim Limit at the level of the individual loan from bank to CDFI rather than at the level of the bank's portfolio, ensuring that each CDFI borrowing from a bank shares the risk in proportion to their take-up of capital from that bank.

- It sets the criterion for a claim against EFG in relation to the performance of the CDFI's portfolio of on-lending rather than, as would be the case in a direct comparison with 'conventional' EFG, the failure of the CDFI in the event of losses arising from on-lending.

- The criterion for and limit of the extent of a claim against the EFG guarantee is that: where there is an overall loss at maturity of the CDFI's portfolio, net of any recoveries made according to their normal loan management procedures **(and net of any direct claims against the EFG guarantee made by the CDFI on individual loans to SMEs, if the CDFI is itself an accredited EFG Lender)**, leading to a shortfall in the CDFI's capital repayments due to the bank.

- In the event of such a loss, the bank is entitled to claim 75% of the shortfall in capital repayments due from the CDFI up to the Claim Limit (say 13%, as in 2010/11). The CDFI is responsible for covering the remaining 25% of the shortfall up to the 13% Claim Limit and 100% of the shortfall beyond the 13% Claim Limit.

- For example, a £1m bank facility to a CDFI will have a Claim Limit of 9.75% (being 75% of a Claim Limit of 13%), translating into £97,500. If the CDFI has net losses of £100k on the £1m facility, then it will be able to claim the full 75%, or £75k. If losses are £200k then the CDFI's claim will be limited to £97,500, rather than £150k (being 75% of £200k).

4.2 Frequently Asked Questions

How is this different?

CDFIs (which, as financial intermediaries, were previously excluded from receiving EFG-backed loans to finance their own lending) are now eligible for EFG loans for the purpose of providing capital for on-lending.

How will this work where a CDFI is also an accredited EFG Lender?

There will be no change as EFG will operate independently at each level (bank to CDFI and CDFI to SME). This will ultimately provide additional security for banks' lending to EFG accredited CDFIs.

Does a CDFI need to be an EFG accredited EFG Lender to receive a bank loan guaranteed under EFG?

Banks can lend to CDFIs whether they are EFG accredited or not. CDFIs will, however, need to demonstrate to the bank that they will be able to repay the loan.

If the CDFIs are lent funds with an EFG loan, can they make a loan which is part funded with other public funding? For example, a loan of £50k which could be funded £25k bank (EFG), £12.5k ex-RDA and £12.5k ERDF?

In the case where a CDFI blends capital from a number of sources in one loan then for the purposes of EFG-backed bank lending to CDFIs the calculations done in the event of default would simply need to be done on a pro-rata basis. Once public funds (in this case from an RDA and ERDF) have been loaned out and then repaid, they are classified as having been recycled. When such recycled money is re-lent by the CDFI, the CDFI will be able to claim against any defaults on loans with this money, and any loans using such funds can count towards raising the Claim Limit (see also section 4.4 on mixing funds).

The benefit to the bank under the guarantee is only accrued in relation to that proportion of the defaulting loan that was made using capital the bank had loaned to the CDFI.

Can a CDFI draw down the loan over time so they can use it to meet on-going requirements for capital?

As with any EFG loan the draw down profile and any other conditions are a matter for negotiation between the bank and the CDFI, provided that the loan remains within the overall eligibility criteria.

Is there a limit on the amount that can be borrowed by a CDFI under the scheme?

It is £1m, the same as for any other EFG Borrower.

Now that CDFIs can borrow in this way under EFG are there any restrictions on their use of the funds borrowed?

Funds borrowed from a bank through this mechanism must be used as capital for on-lending to SME customers of the CDFI. If a CDFI (like any other business) wished to borrow for working capital or investment project purposes then it should apply for a bank loan in the normal way and the Lender will decide whether or not it wishes to lend, including deciding whether or not it is appropriate to make that loan with the backing of EFG.

Banks often require Personal Guarantees and / or other security to be provided from the Directors of a business before they are prepared to lend, including under EFG. Will similar guarantees be expected from a borrowing CDFI's Directors?

The taking of Personal Guarantees from Borrowers is a commercial matter for the Lender and not an eligibility condition of EFG. In all lending decisions the availability of security, including the provision of Personal Guarantees, will be explored by the Lenders. However, in most cases where banks have established relationships with CDFIs there is an understanding of the differences between the role and status of the management of the CDFI compared with that of an owner-managed profit-distributing small business.

Won't this mean that banks will make inappropriate (high risk) loans to CDFIs?

This provides an additional guarantee for banks but the CDFI will still need to demonstrate to the bank that it has appropriate lending procedures and is capable of servicing the loan. Lenders will still be exposed to risk and so it will not be in their interests to make inappropriate loans to CDFIs which they do not have confidence in.

Won't banks only want to lend to CDFIs who are EFG accredited?

This is a commercial decision for the bank and will be informed by Lenders' assessments of applications for loans of capital for on-lending from CDFIs. Any CDFI which a bank deems credible can benefit.

Will there be a cap on what the banks can claim on the loans they make to CDFIs under the scheme?

The normal EFG Claim Limit will apply. However, the cap will operate at the level of each individual loan from a bank to a CDFI. This is to ensure that all participating CDFIs remain directly accountable for their borrowing and to aid implementation.

Say the Claim Limit on money lent to CDFIs from banks will be 13% (as in 2010/11) and the guarantee rate 75%, both as in 'conventional' EFG, meaning that the total amount claimable by the bank on each EFG loan to a CDFI will be 9.75% of the amount drawn and on-lent by the CDFI.

How will the bank claim against the EFG for these loans? Won't it mean CDFIs going into administration?

The bank will claim based on the performance of the CDFI's portfolio of loans made from the capital provided by the bank. The Lender will make a single claim either on maturity (full repayment) of the loan to the CDFI, or sooner if the threshold for the maximum possible Claim (see above) is reached while the portfolio of on-lending by the CDFI is still active. It is for the bank to determine the level of monitoring information it requires from the CDFI on the performance of the portfolio of on-lending in order to determine when and how much to claim.

Can a bank benefit from Community Investment Tax Relief (CITR) on an EFG loan to a CDFI?

Yes, subject to the CITR rules being satisfied. In practice the principal restriction to be taken into account is that the CDFI is not entitled to then on-lend those funds as EFG loans and treat them as a relevant investment for CITR purposes. More details on CITR can be found in section 4.5 below.

4.3 Worked Examples

Example 1: CDFI is NOT an accredited EFG Lender

Amount borrowed by CDFI for on-lending (£)	500,000
EFG Guarantee Rate (%)	75
EFG Claim Limit (%)	13

Performance of CDFI's Portfolio of On-lending					
Loan Reference	**Loans by CDFI to Clients (£)**	**Repaid in Full?**	**Balance Outstanding at Default (£)**	**Subsequent Recovery by CDFI (£)**	**Net Loss to CDFI (£)**
1	30,000	Y	0	0	0
2	20,000	N	5,000	0	5,000
3	50,000	N	25,000	5,000	20,000
4	50,000	N	25,000	2,500	22,500
5	50,000	Y	0	0	0
6	25,000	Y	0	0	0
7	25,000	N	10,000	0	10,000
8	75,000	N	35,000	10,000	25,000
9	30,000	Y	0	0	0
10	20,000	Y	0	0	0
11	50,000	Y	0	0	0
12	25,000	N	20,000	2,500	17,500
13	40,000	Y	0	0	0
	490,000		**120,000**	**20,000**	**100,000**

Maximum shortfall against which bank may claim (£) *(Cap Rate % of Amount Drawn and On-Lent by CDFI)*	(£490k * 13%)	63,700
Maximum possible claim which bank may make (£) *(Pro-rata on Shortfall at Guarantee Rate %)*	(75% * £490k *13%)	47,775
Shortfall between capital borrowed by CDFI from bank and repayments of capital to CDFI by SMEs (£)		100,000
Actual claim made by bank (£) *(Lesser of maximum possible claim and guaranteed percentage of net loss incurred by CDFI on portfolio)*		**47,775**
Amount to be found by CDFI to repay remainder of loss to bank (£)		52,225
Total loss carried by CDFI (£)		**52,225**

Example 2: CDFI is an accredited EFG Lender and uses EFG in some on-lending of EFG-backed bank capital

Amount borrowed by CDFI for on-lending (£)	500,000
EFG Guarantee Rate (%)	75
EFG Cap Rate (%)	13
CDFI's own EFG Claim Limit available (£)	25,000

Performance of CDFI's Portfolio of On-lending

Loan Reference	Loans by CDFI to Clients (£)	Repaid in Full?	Balance Outstanding at Default (£)	Subsequent Recovery by CDFI (£)	Loan Guaranteed under CDFI's own Accreditation? (If "Y" then capital does NOT qualify for CITR)	Loss to CDFI prior to claim under own EFG Claim Limit (£)	EFG Claim by CDFI (£)	Loss to CDFI (£) (Including CDFI's 25% risk on own EFG loans and any further shortfall following exhaustion of own EFG Claim Limit)	Losses Eligible for "transferring" to count towards bank claim against EFG Claim Limit
1	30,000	Y	0	0	N	0	0	0	0
2	20,000	N	5,000	0	Y	5,000	3,750	1,250	0
3	50,000	N	25,000	5,000	N	20,000	0	20,000	20,000
4	50,000	N	25,000	2,500	Y	22,500	16,875	5,625	0
5	50,000	Y	0	0	N	0	0	0	0
6	25,000	Y	0	0	Y	0	0	0	0
7	25,000	N	10,000	0	N	10,000	0	10,000	10,000
8	75,000	N	35,000	10,000	Y	25,000	4,375	20,625	14,375
9	30,000	Y	0	0	N	0	0	0	0

10	20,000	Y	0	0	Y	0	0	0	0
11	50,000	Y	0	0	Y	0	0	0	0
12	25,000	N	20,000	2,500	Y	17,500	0	17,500	13,125
13	40,000	Y	0	0	N	0	0	0	0
	490,000		**120,000**	**20,000**		**100,000**	**25,000**	**75,000**	**57,500**

Maximum shortfall against which bank may claim (£) *(Cap Rate % of Amount Drawn and On-Lent by CDFI)*	(£490k * 13%)	63,700
Maximum possible claim which bank may make (£) *(Pro-rata on Shortfall at Guarantee Rate %)*	(75% * £490k * 13%)	47,775
Shortfall between capital borrowed by CDFI from bank and CDFI's direct ability to repay bank (£)		75,000
Actual claim made by bank (£) *(Lesser of maximum possible claim and guaranteed percentage of bank's eligible losses arising from CDFI portfolio)*	(75% * £57,500)	**43,125**
Amount to be found by CDFI to cover bank's "25%" loss arising from EFG lending to CDFI (£)	(£57,500 - £43,125)	14,375
Amount to be found by CDFI to cover direct loss arising from own EFG lending repayable to bank (£)	(£75,000 - £57,500)	17,500
Total loss carried by CDFI		**31,875**

NB: This example assumes that the CDFI has its own EFG accreditation which it has used to cover identified loans in this portfolio and others in other portfolios, and that £25k of the CDFI's own claim limit is available for use in connection with this portfolio. Demands are assumed to occur in the order in which the loans are listed, meaning that the full 75% is claimable in relation to the first two "own EFG" Demands (Loans 2 & 4), a partial claim is possible on the third (Loan 8) and no claim is possible on the fourth (Loan 12). In all four cases the CDFI bears the first 25% of the loss incurred.

Further Detail re. Loan 8: Loss to CDFI is £25k. As loan is made under the CDFI's own EFG accreditation the loss is split 25% CDFI : 75% EFG = £6,250 : £18,750. But the CDFI only has £4,375 of own EFG Claim Limit remaining. EFG shortfall of £14,375 (£18,750 - £4,375) is therefore "transferable" to the losses eligible for inclusion in the bank's claim against its own EFG Claim Limit.

4.4 Mixing Eligible and Non-Eligible Funding Sources

In addition to appraising the eligibility of the Applicant for EFG, CDFIs and other smaller lenders also need to consider the eligibility of their own funds to be lent under the EFG programme. Funding sources for CDFIs are often from a mix of public and private sources, including local authority grants, ERDF funds and ex-RDA funds inter alia, as well as funding provided on a commercial basis (see section 4.5 for CITR restrictions).

CDFIs and other smaller lenders are responsible for each checking the eligibility of such funding to be on-lent with the backing of EFG. It is often the case that the first loan made from a funding source may not qualify for EFG backing, but will do so when it has been recycled. In some instances, the funding may only qualify once the funds have been recycled twice.

Where a portion of a CDFI's or smaller lender's funds are ineligible for EFG, the CDFI or smaller lender must determine how eligible and ineligible funds are being channelled into individual investments. For example, a CDFI or smaller lender has a total fund of £1m but only £200k is eligible for EFG support. Where the CDFI or smaller lender does £300k of lending and all cases are eligible for EFG – the CDFI or smaller lender will need to be clear whether it has done either £200k of EFG lending plus £100k of non-EFG lending, or £300k of lending where only 20% of each individual facility has the backing of the EFG.

4.5 Use of CITR and EFG

4.5.1 Introduction

The Community Investment Tax Relief ("CITR") scheme is intended to stimulate private investment in disadvantaged communities by providing a tax incentive to individuals and companies that invest in accredited CDFIs.

The tax relief is worth up to 25% of the value of the investment in the CDFI and is spread over five years, starting with the year in which the investment is made.

A CDFI that receives capital that benefits from CITR ("CITR Funding") may not lend using EFG unless it has met certain thresholds with regards to non-EFG lending. In all, the value of EFG lending is restricted to approximately 25% of the CDFI's fund (see below). However, an investment which benefits from CITR can also be in the form of an EFG loan from an accredited Lender to the CDFI.

HMRC has published a comprehensive online manual with regards to CITR which can be found here: www.hmrc.gov.uk/manuals/citmanual.

4.5.2 Restrictions on EFG Lending when using CITR Funding

Under SI2003/96 Regulation 8, all CDFIs must invest most of their CITR Funding in "Qualifying Enterprises" (such as those focussed on disadvantaged geographies or demographics), and the investments themselves must be "Relevant Investments" which includes most loans and equity investments, but does not include EFG facilities.

The required levels of onward investment in Relevant Investments in Qualifying Enterprises increases over the years that follow the date on which the CDFI was first granted accreditation. Within the first year 1, 25% of the CDFI's fund must be invested in Relevant Investments in Qualifying Enterprises. Within two years and three years at least 50% and 75% (respectively) of the investment fund must have been so invested. In practice, unless the CDFI is making very short term investments, it will be restricted to ensuring that the value of its EFG backed facilities does not exceed 25% at any stage.

As EFG is designed to stimulate lending above and beyond a Lender's normal lending output, BBB would envisage that EFG facilities will represent less than 25% of a CDFI's fund in the majority of cases.

For example, a CDFI lender has a capital funding pot of £1m of which £500k benefits from CITR. The remaining £500k comes from an eligible (for EGF) funding source. In practice, the CDFI lender has only £625k of funding (£500k + £125k (£500k x 25%)) that can be used for EFG.

Section CITM3010 of the HMRC manual gives further guidance on the calculations involved with regards to the size of the fund and the investments that it makes.

5 The EFG Application Process Using the EFG Web Portal

5.1 Quick Reference Guide

The following table summarises the key stages of the application process using the EFG Web Portal.

The EFG Web Portal Manual is available to all Web Portal users. However, this chapter provides an overview of the end-to-end operational process for the provision of an EFG loan.

Reference is given to the loan status (on the EFG Web Portal) and the changes that are made to the Web Portal at each stage (more information on Web Portal states is provided in section 5.2). Additionally the table summarises the timing rules that are applicable at each stage of the application process.

	Key Stages	Process and Status	Timing Rules	Ref
1	Initial Appraisal of the Borrowing Proposal	Initial appraisal of lending proposition to be considered for EFG. Lender must be comfortable that the proposition is viable, but that absence or inadequacy of security makes the proposal unsupportable.		5.3.1
2	Check Eligibility	Check Eligibility via Web Portal. Facility status recorded as ***Eligible.***	***Eligible*** status will automatically expire if not ***Cancelled*** or progressed to ***Complete*** on the Web Portal within 6 months.	5.3.2
3	Credit Approval (May precede Stage 2 – depending on Lender's process)	Application approved under local discretion or referred to internal credit team to obtain sanction depending on Lender's processes and criteria.		5.3.3

4	Data Protection and Disclosure Declaration	Lender must ensure that they have authorisation from customer to disclose information to BIS via Web Portal. In most cases an authorisation will already exist but a downloadable Data Protection and Disclosure Declaration is available from the Web Portal.		5.3.4
5	Completing the Application	Enter remaining customer and facility details in order to update the facility status to ***Complete***.	***Complete*** status will automatically expire on the Web Portal if not ***Cancelled*** or ***Offered*** within 6 months.	5.3.5
6	Print and Issue Documentation for Customer Completion and Acceptance	• Facility Letter (Lender's own document but must include EFG-specific clauses, such as the Premium) • Direct Debit Mandate (available from Web Portal but Lender may keep stock of paper forms) • Information Declaration (from Web Portal) • State Aid Letter (from Web Portal) • Premium Schedule (from Web Portal) • Security Charges (Lender's own documentation – when applicable)	Facility Letter Date cannot precede the date of progress from ***Eligible*** or ***Incomplete*** to ***Complete*** by more than thirty days.	5.3.6
7	Offer Facility to Applicant	When all documentation has been issued update the facility status to ***Offered.***	Portal status must be updated to ***Offered*** within 10 business days of Facility Letter Date.	5.3.7
8	Facility Drawn Down and Guaranteed	When completed documentation is received back from the customer (and, if appropriate, charges over security have been perfected) the Lender may release the funds and update the facility status to ***Guaranteed***. Lender is responsible for sending a copy of the Direct	The guarantee lapses if facility is not drawn within 6 months. Lenders may set shorter acceptance periods in accordance with their own commercial practices. Web Portal status must be updated within 10 business days of draw	5.3.8

		Debit mandate to the Borrower's bank (account from which Premium will be paid) and details of the EFG Guarantee Premium to the Premium Collection Agent (the "PCA").	down (and 10 business days of any subsequent tranche draw down).	
9	Repayment and Closing Facilities	When loan is repaid, update facility status to ***Repaid***.	Web Portal status must be updated to ***Repaid*** within 10 business days of the repayment.	5.3.9

5.2 Different EFG States and the Web Portal

Throughout its life on the EFG Web Portal, an EFG facility will be in one of a number of "states", including the following:

State	**Meaning**
Eligible	Application has been loaded on the Web Portal on an anonymous basis and basic eligibility checks undertaken, with a positive result.
Incomplete	A signed Data Protection and Disclosure Form is held. Business and facility details have been entered into the eligibility check but some details remain outstanding.
Complete	Full business and facility details have been provided and a full eligibility check undertaken. This stage provides the definitive ruling on whether an EFG Application is eligible.
Offered	Facility Letter plus all other EFG documentation has been prepared and forwarded to the Applicant. Lenders have 10 business days to change the status of an application to "Offered" once the documentation has been sent out to an Applicant.
Guaranteed	EFG offer has been accepted by the Borrower and the facilities have been "Guaranteed".
Drawn	Once the Borrower has accepted the EFG offer and has drawn down at least an initial tranche of funds, the Lender has 10 business days to update the Web Portal to show the current status of the applicant as Drawn.

Repaid	Once the EFG facility has been fully repaid by the Borrower, the Lender has 10 business days to update the Web Portal to show the current state of the Borrower as Repaid.
Lender Demand	If the Lender has made Demand on the Borrower for repayment of the EFG facility, the Lender has 10 business days to update the Web Portal to show the current state of the Borrower as Lender Demand.
Guarantee Demand	For delinquent EFG facilities, once the Lender has satisfied all security realisation procedures and / or reached 18 months after Lender Demand, the Lender can make Demand upon the guarantee from BIS (a "Claim on the Guarantee").
Settled	Payment under the guarantee has been made by BIS.
Recovered	Any money recovered from the Borrower by the Lender (for example, via realisation of security) to be paid back to BBB (BIS).

For a full listing of Web Portal EFG "states" – see Web Portal Manual v.3 (section 4.1).

5.3 Typical EFG Application Process

5.3.1 Initial EFG Appraisal

- Applicant and RM discuss borrowing proposal.
- The Lender must be comfortable that the proposition is viable, but that absence or inadequacy of security makes the proposal unsupportable.
- Applicant will need to provide all the information normally required by a Lender in connection with a normal borrowing proposal, typically including:
    - Business Plan – including details of the purpose of the facility and details of other borrowings of the business;
    - Suite of financial information – to include historic trading figures, management accounts and financial projections;
    - Details on any other publicly funded support received by the business within the past three years; and,
    - Details of any security available – business or personal – to secure the borrowing proposal.

- RM will look to provide a normal commercial borrowing facility wherever possible but can consider using EFG if:

    - the applicant appears viable and the borrowing can be repaid;
    - no or insufficient security is available to meet the Lender's normal security requirements; and,
    - the borrowing proposal meets basic EFG eligibility criteria as detailed in section 2.

5.3.2 Check Eligibility

- The RM will assess eligibility against the basic criteria directly or in consultation with the Lender's central EFG processing team who can provide guidance and load the basic details of the proposal onto the EFG Web Portal. At this stage, the process is anonymous.

- For some Lenders, the RM would, at this stage, complete a deal pro-forma and forward this through to the Lender's central processing team for EFG so that the proposal can be loaded onto the Web Portal and eligibility officially confirmed or otherwise. The Applicant would need to give permission to allow their details to be entered onto the Web Portal. Details regarding any existing State Aid provided to the Applicant must also be obtained.

- If rejection is at the Web Portal eligibility stage, the Web Portal will provide a reason for the rejection, which the RM should feed back to the Applicant. The Web Portal will automatically record details of all rejected EFG applications.

5.3.3 Credit Approval

- Credit approval may precede Stage 2 – dependent upon Lender's process.

- The RM will prepare a credit application and obtain credit sanction for the borrowing proposal.

- Upon receipt of credit sanction, the RM will complete some form of application form / pro-forma to provide all of the necessary information on the transaction for entry on to the EFG Web Portal by the central processing team, including details of any support received from other public programmes which constitute State Aid.

- If the Application is rejected by the Lender at the viability stage (by the RM or credit sanctioner), then this is a commercial decision by the Lender and should be presented as such to the Applicant. If the Applicant is unhappy with the decision made, the Applicant should be advised to follow the Lender's normal complaints procedure with escalation to the Financial Ombudsman if deemed necessary by the Applicant.

5.3.4 Data Protection and Disclosure Declaration

- If they haven't already done so, the Applicant must give permission, using the EFG Data Protection and Disclosure Form (or similar) to allow their business details to be entered onto the EFG Web Portal. The wording of this Declaration should follow a standard format – see Appendix 9.1.

- The RM pro-forma plus the Applicant's Data Protection and Disclosure Form are forwarded to the central processing team for input onto the EFG Web Portal.

5.3.5 Completing the Application

- Enter remaining customer and facility details and update the facility status to Complete.

5.3.6 Print and Issue Documentation

- Once eligibility is confirmed, the central processing team will produce the following documentation from the EFG Web Portal.

The State Aid Letter

- The State Aid Letter is used to inform the Applicant how much *de minimis* State Aid has been received relating to the facility guaranteed within the EFG scheme.

- The amount of *de minimis* State Aid, calculated using the Premium Payment and State Aid Calculator, is added to the State Aid Letter and should be sent to the Applicant when the EFG scheme facility is offered. See Appendix 9.2 for a sample letter.

The Premium Schedule

- See section 6.5 for full details on the collection of the Premium payments.

- Premiums are due on all facilities that have been guaranteed and drawn within the EFG scheme. For term loans, the Premium is based on the outstanding balance of the EFG loan throughout its term. For Overdraft Guarantee and Invoice Finance Guarantee facilities, the Premium is calculated on the maximum lending limit allocated to the Borrower, irrespective of utilisation level.

- To calculate the Premium payments required for an EFG application, use the Premium Payment and State Aid Calculator within the Web Portal.

- This information should then be distributed to the Applicant to allow them to understand what their financial obligations are during the facility term.

- See Appendix 9.3 for a Premium Payment Schedule sample letter.

- In addition, the Premium Payment and State Aid Calculator identifies the amount of *de minimis* State Aid applicable for the EFG facility, which needs to be entered into the EFG Web Portal and entered onto the State Aid Letter to inform the Applicant of the amount of State Aid applicable for the new EFG facility.

Direct Debit Mandate

- Premium payments are paid using direct debit. In order to put the EFG Scheme Facility and related Scheme Guarantee in place, a Direct Debit Mandate must be completed by the Applicant. The mandate is available in the Web Portal.

- See section 6.5 for full details on the collection of the Premium payments.

Information Declaration

- The Information Declaration confirms to the Applicant all information entered onto the Web Portal by the Lender. The Information Declaration has space for two signatories. The Information Declaration should include the same Borrower signatures as those that are on the Facility Letter and, therefore, there may be the need for one signature or, in some cases, two or more signatures. See Appendix 9.4 for a sample letter.

Facility Letter

- The central processing team also often produces the Facility Letter for the new EFG facility although this is sometimes created by the RM. **Note that the Facility Letter must contain additional clauses relating to the payment of the Premium, in accordance with the EFG Legal Agreement.**

- Typically, these additional clauses are:

    - that the Secretary of State has agreed under Section 8 of the Industrial Development Act to guarantee the Borrower's payment obligations or the amount outstanding, under the scheme facility on the terms agreed between the Lender and the Secretary of State and subject to the payment by the Borrower of the Scheme Guarantee Premium;
    - that the Borrower shall pay to the Secretary of State quarterly payments of the Scheme Guarantee Premium, at such times and in such manner as the Secretary of State may require, the due date and amount of each such payment being as specified in the Premium Payment Schedule;
    - that the Lender shall at all times be entitled (but not obliged) to pay any sum due from the Borrower to the Secretary of State in respect of the Scheme Guarantee Premium under the Facility Letter and the Borrower shall forthwith on demand reimburse the Lender for any sums paid by the Lender to the Secretary of State in that respect;
    - that the Borrower's undertakings to pay the Scheme Guarantee Premium are expressed to be for the benefit of, and to be enforceable by, the Secretary of State notwithstanding that the Secretary of State is not a party to the Facility Letter; and,
    - that the Borrower shall not be permitted to make any drawdown under the scheme Facility Letter or make any utilisation of the increased scheme facility, unless and until the Borrower provides a satisfactory means of payment of the first instalment of the Scheme Guarantee Premium and returns the Direct Debit Mandate and the Information Declaration to the Lender, each duly signed, dated and completed, and, as regards the Information Declaration, without any amendments or variations having been made to the information contained therein (if the Information Declaration is returned by the Borrower with any amendment or variation to the information contained therein or the Borrower informs the Lender, having received such Information Declaration, that any of the information contained therein needs to be amended or varied then other provisions shall apply).

Security Charges

- If additional security is required as a consequence of granting the EFG facility, this will be instructed by either the RM or a central processing team who will monitor progress pending completion of the security charging process.

5.3.7 Offer Facility to Applicant

- All documentation is then forwarded to the Applicant for signature and return.

- The Lender, having made the offer of the EFG facility, must update the Web Portal as soon as reasonably practicable but in any event within 10 business days of the date of the offer.

5.3.8 Facility Drawn Down and Guaranteed

- Once the facility documentation has been signed and returned by the Applicant and where necessary, all security procedures have been completed, the EFG facility will then be drawn down and the Web Portal updated to Guaranteed (within 10 business days of draw down).

- The availability period allowed for draw down of the EFG facility should reflect the Lender's normal business practice, subject to a maximum period of 6 months. For example, if the Lender normally allows one month for acceptance of the offer and three months thereafter for drawdown, the terms of the EFG facility should reflect this standard practice.

- If the Applicant draws down the EFG facility in tranches, with the first tranche only drawn within 6 months, there is not a new time limit for drawing down the remainder of the EFG facility. The period allowed for drawdown is subject to the Lender's normal criteria and agreement with the Applicant, as set out in the facility letter.

5.3.9 Repayment and Closing Facilities

- When the loan is repaid, the Web Portal status must be updated to "Repaid" within 10 business days of the repayment. It is also the Lender's responsibility to cancel the direct debit.

- Partial repayments are permissible. If a partial repayment is made outside the normal repayment profile agreed for the facility then the Lender must update the Web Portal and recalculate the Premium Schedule, advising the customer accordingly.

- Recalculation must be performed as soon as practically possible after repayment has been received, noting that any change will be effective from the next quarterly Premium collection.

5.4 Adjusting Facility Details Prior to Loan Drawdown

5.4.1 Adjusting the Interest Margin

The interest rate can be changed at any time until the loan is "Offered", at which point a formal Facility Letter must have been produced. Between this point and draw down, the loan details cannot be changed. The Offer is effectively "locked down" in the EFG Web Portal and there is no facility within the Web Portal to change the margin. In practice, however, if the Lender wishes to change the margin, they may do so though such a change cannot be recorded against the EFG facility details on the Web Portal.

Chapter 9 of the Web Portal Manual v.3 addresses how to update the Web Portal after the loan details have been completed.

5.4.2 Adjusting the Facility Amount

The facility amount can be changed at any time until the loan is "Offered", at which point a formal Facility Letter must have been produced. The Lender's ability to change the facility amount will depend upon whether a decrease or increase in the facility amount is required.

For a reduction in the facility amount, the Lender can take the original facility offer to "Guaranteed" and then go to the "Change Amount or Terms" screen within the Web Portal, register a lump sum reduction in the facility amount and proceed with the EFG facility at the new lower amount. A revised Premium Schedule would need to be generated and forwarded to the Borrower.

If a higher facility amount is required, then the Lender must either reject the original facility offer and start the process again, or proceed with the original facility through to "Guaranteed" and then offer the additional amount as a new top-up EFG facility.

If the Lender wishes to change the facility amount prior to drawdown, the existing "Offered" loan should be "Cancelled" on the Web Portal and a new loan application processed.

5.4.3 Adjusting the Term or Repayment Profile

If the scheduled final date for repayment of the EFG facility is likely to change, this must be recorded on the Web Portal.

Early repayment of an EFG facility is permissible. Early repayment charges are subject to the Lender's normal charging criteria. However, no further EFG Premiums will be collected after the Lender has updated the Web Portal to advise that the EFG facility has been "Repaid" and the Borrower has been advised to cancel their direct debit payment.

The repayment profile can be changed at any time until the loan is "Offered". Once "Guaranteed", further changes can then be made using the "Change Amount or Terms" screen in the Web Portal where alterations to the repayment profile can be made. A revised Premium Schedule will also need to be generated and forwarded to the Borrower.

Again, if the Lender wishes to change the facility term or repayment profile prior to drawdown, the existing "Offered" loan should be cancelled on the Web Portal and a new loan application processed.

Once a term loan has been repaid it is "Closed" and cannot be redrawn. Should more funds be required a new facility needs to be applied for. Similarly, should a tranche of a loan be repaid (early or otherwise) it cannot be redrawn – a fresh application needs to be made. Utilisation of invoice finance and overdraft facilities can fluctuate up to the prevailing agreed maximum limit throughout their terms.

5.4.4 Deciding Not to Make an Offer

If a Lender offers an EFG facility to an Applicant, but decides subsequently to withdraw the offer, the Applicant should be informed and the Web Portal updated accordingly (change the facility status to show "Loan Cancelled").

5.5 20 Day Response Target

On 1 August 2010, a 20 business day processing target for EFG proposals was introduced. This target has been adopted by all of the main High Street banks and also some of the smaller EFG lenders.

The clock for the 20 business days starts when all necessary information has been provided by the SME and / or their advisors such that the Relationship Manager ("RM") is in a position to prepare a credit application. If customer-specific due diligence needs to be undertaken prior to the credit application being prepared, then the clock will start once that due diligence has also been completed.

The 20 business days will include the time taken for preparation of the credit application, sanctioning of the credit application, through to production of an Offer (or Decline) Letter for the SME. The 20 day target is measured to the provision of an Offer Letter and not to draw down of funds.

In order to accurately calculate turnaround times on applications, and recognising that the point of interface between the commercial lending process and the EFG Web Portal process varies between Lenders, there is a requirement to record on the Web Portal the date on which the RM received a fully documented borrowing proposal from the SME. **This date should be recorded during the Loan Entry stage of the Web Portal process in dd/mm/yyyy format in the fourth Lender-defined field.**

We would suggest that, in order to have both a clear audit trail and also supporting evidence in the event of any future dispute on processing time between the SME and the Lender, Lenders should ensure that a mutually agreed start date for each proposal is recorded, for example, by the SME and RM both signing the application form to confirm that all documentation was provided on a specific day. Precisely how the capture of an agreement to this start date might best be achieved is a matter for each individual Lender to determine.

The emphasis is on the Lender, and specifically the RM, to ensure that the SME is aware from the beginning of the borrowing relationship what information they and / or their advisors must provide in order that a credit application can be prepared and considered. Where necessary, the RM should consult with their credit department in advance to ensure all necessary information is requested upfront by the RM. In-line with existing good practice, the RM should advise the SME upfront on the different stages involved in the application process and likely timescales. Where a Lender's credit department subsequently requests that the RM obtains additional information from the SME and / or their advisors before the application can be progressed, the clock for the 20 day turnaround should not be stopped.

In the event of BIS or BBB receiving complaints from individual SMEs on the time taken to process an EFG application these will be referred to the operational lead for each Lender.

6 Managing EFG Facilities once the Guarantee is in Place

6.1 Refinancing EFG Debt from Another Lender

6.1.1 Refinancing EFG Debt – Introduction

Often when switching Lender, a business will need to negotiate new borrowings from Lender B (to which the business is moving) **specifically in order to repay existing lending** provided by Lender A (which the business is leaving). It is possible in such cases that **the original lending provided by Lender A is EFG-backed and the new lending from Lender B to replace it also satisfies the EFG eligibility criteria.**

The EFG guarantee **cannot be transferred or reassigned** between Lenders. In the event that a Borrower with an EFG-backed facility switches Lender then it is for the new Lender to decide whether it is necessary or appropriate to use EFG in order to facilitate the new package of lending to be provided to their new customer. Existing EFG-backed facilities provided by the original Lender must be repaid and then the new Lender must process a new EFG application for any qualifying facility they intend to provide. These arrangements ensure appropriate treatment of both Lenders in respect of the Annual Claim Limit.

As reported in section 2.5.2 the eligibility rules regarding *de minimis* State Aid require that no business (or group) can a) have EFG facilities of over £1.2m outstanding at any one time and b) receive no more than €200,000 of State Aid (or lower ceiling where sectorally applicable) over a rolling three-year period. As an EFG facility cannot be transferred between Lenders, the implication is that re-applying for a comparable EFG facility would count towards the €200,000 rolling three-year State Aid limit.

The practical arrangements described below are, therefore, intended to ensure that the presence of EFG does not act as a barrier to the freedom of businesses to switch between Lenders. Where the practical arrangements are followed, then any contribution towards the €200,000 rolling three-year State Aid limit arising from the issue of the replacement EFG facility can be ignored.

6.1.2 Practical Arrangements

These arrangements apply specifically in connection with Lender B providing an EFG-backed facility to a switching Borrower which previously had an EFG-backed facility from Lender A, in order for the Borrower to be able to fully repay the balance of that facility to Lender A.

They are, therefore, limited to an EFG-backed facility provided by Lender B which:

- Is for a **value not exceeding the outstanding capital balance** of the previous facility from Lender A at the point of switching, which itself may not exceed the original value of the facility when first provided by Lender A. For the avoidance of doubt, no outstanding interest, early redemption penalties or other charges may be added to the EFG-backed loan provided by Lender A. Any additional borrowing requirements identified by Lender B at the time of switching or thereafter, in connection with which the use of EFG may be appropriate, must be considered as a separate transaction.

- Once the replacement loan has been created it can then be extended. However, the lending should be over a term which, when combined with the elapsed term of the previous facility provided by Lender A, does not exceed the maximum permitted term for the type of facility involved. For the avoidance of doubt Lender B is allowed to extend the term of the facility to the maximum term permitted for that type of facility. For example, a business originally had an 8-year term loan with Lender A. After 5 years it moves to Lender B so Lender B provides a loan covering the outstanding balance over the remaining term of 3 years. Lender B subsequently agrees to an extension. The maximum extension Lender B is entitled to offer is 2 years (NOT 7 years).

Note that this treatment is specific to EFG and does not apply to SFLG.

6.1.3 Web Portal Adjustments

Further information on how to update the Web Portal in respect of refinancing debt from another Lender can be found in the Web Portal Manual v.3 section 12.0. The following should be considered:

For Lender A:

- On receipt of the funds from Lender B the facility should be reported as "Repaid".
- As a courtesy, Lender A should remind their former customer of the need to cancel their Direct Debit Mandate.
- Lender A now has no further entitlement to claim against the Guarantee.
- The "contribution" of the facility to Lender A's Claim Limit remains unchanged.

For Lender B:

- The fact that the switching Borrower had previously been provided with an EFG-backed facility by Lender A does not remove the requirements for Lender B to undertake their normal commercial due diligence and to establish that it remains appropriate to provide the Borrower with an EFG-backed facility on this occasion.
- Each case should be entered as a new application and processed through to "Guaranteed" and "Initial Draw" in the usual manner, paying particular attention to the variations to standard procedures detailed below.
- There is no need to issue a replacement State Aid Letter for the replacement facility. However, the Borrower should be advised that their existing State Aid Letter is still in force. The Lender should make a file note explaining why no letter has been issued.
- For the avoidance of doubt, these instructions provide the practical authorisation for Lenders to apply the variations listed in the handling of qualifying cases.

Lenders should expect that a sample of such cases will be audited in future cycles of Lender Audit.

It is likely to be of assistance to Lender B if, at the time of Application, the Borrower is able to provide a copy of the Information Declaration applicable to their previous borrowing from Lender A.

6.2 Refinancing of Non-EFG Debt from Another Lender

Credit assessment and risk appetite will vary between Lenders and it is natural for Borrowers to consider alternative sources of finance. EFG is not to be used by a Lender as a mechanism for building market share. However, when taking on a new customer's debt, EFG may be appropriate and it is therefore permissible for one accredited Lender to use an EFG to take on a business' non-EFG debt that has been held by another accredited Lender. These circumstances would not be viewed as refinancing for the purposes of Type C or Type D EFG.

6.3 Changing Legal Status of the Borrower or Facility Purpose

6.3.1 Changing Legal Status

Applicants occasionally have an existing EFG (or SFLG) loan and then subsequently wish to change legal status. For most Lenders, a change of legal status of the Borrower (for example, from sole trader to limited company) would require a revised credit application with a reassessment of security requirements (for example, a Personal Guarantee may be required when legal status changes from sole trader to limited company), a change of facility and security documentation and a change in the name of the bank account.

Assuming no increase in borrowing is required, existing debt would be repaid and then re-drawn in the name of the new borrowing entity. Where an existing SFLG loan is in operation, this would also need to be repaid as part of the change of name of the borrowing entity. The borrowing would then need to be re-drawn as an EFG loan – the terms and conditions of the EFG loan may or may not be the same as for the old SFLG loan, depending upon the Lender's credit criteria at that point in time.

For an existing EFG loan, this would also need to be repaid and a new EFG loan drawn – again, the terms and conditions of the new EFG loan may or may not be the same as the old EFG loan, depending upon the prevailing credit assessment of the Lender. These circumstances would not be viewed as refinancing.

As discussed, the eligibility rules require that no business (or group) exceeds the £1.2m EFG outstanding facility limit and / or the €200,000 rolling three-year State Aid limit. Where the legal status of the Borrower has been changed, but where the fundamental business has not been changed, then the EFG renewal will not affect the position for either limit.

6.3.2 Changing Facility Purpose

On occasion, a Borrower will wish to use an EFG facility for a purpose other than that which was specified in the facility application. This can occur when funds have already been drawn, or when requesting a tranche draw down.

Under such circumstances the Lender must consider whether the facility is still eligible for EFG. If it is, the Lender should make a file note recording the fact that the loan has been reappraised and is still eligible for EFG (in terms of viability, security and the UK SME Test). Under such circumstances, the same EFG will remain in place. Where the loan fails to meet EFG eligibility, no further tranches may be drawn. If the loan has already been drawn, it should be repaid or refinanced by commercial debt.

6.4 Adjusting Facility Details Once Guarantee is in Place

6.4.1 Adjusting the Interest Margin

As stated in section 5.4.1, the interest rate can be changed at any time until the loan is "Offered", at which point a formal Facility Letter must have been produced. Between this point and draw down, the loan details cannot be changed. The Offer is effectively "locked down" in the EFG Web Portal and there is no facility within the Web Portal to change the margin. In practice, however, if the Lender wishes to change the margin, they may do so though such a change cannot be recorded against the EFG facility details on the Web Portal.

Chapter 9 of the Web Portal Manual v.3 provides guidance on how to update the Web Portal after the loan details have been completed.

6.4.2 Adjusting the Facility Amount

Again, the facility amount can also be changed at any time until the loan is "Offered", at which point a formal Facility Letter must have been produced (as stated in section 5.4.2). The Lender's ability to change the facility amount will depend upon whether a decrease or increase in the facility amount is required.

For a reduction in the facility amount, the Lender can take the original facility offer to "Guaranteed" and then go to the "Change Amount or Terms" screen within the Web Portal, register a lump sum reduction in the facility amount and proceed with the EFG facility at the new lower amount. A revised Premium Schedule would need to be generated and forwarded to the Borrower.

If a higher facility amount is required, then the Lender must either reject the original facility offer and start the process again, or proceed with the original facility through to "Guaranteed" and then offer the additional amount as a new top-up EFG facility.

If the Lender wishes to change the facility amount prior to drawdown, the existing "Offered" loan should be "Cancelled" on the Web Portal and a new loan application processed.

6.4.3 Adjusting the Term or Repayment Profile

As stated in section 5.4.3, if the scheduled final date for repayment of the EFG facility is likely to change, this must be recorded on the Web Portal.

Early repayment of an EFG facility is permissible. Early repayment charges are subject to the Lender's normal charging criteria. However, no further EFG Premiums will be collected after the Lender has updated the Web Portal to advise that the EFG facility has been "Repaid" and the Borrower has been advised to cancel their direct debit payment.

The repayment profile can be changed at any time until the loan is "Offered". Once "Guaranteed", further changes can then be made using the "Change Amount or Terms" screen in the Web Portal where alterations to the repayment profile can be made. A revised Premium Schedule will also need to be generated and forwarded to the Borrower.

Again, if the Lender wishes to change the facility term or repayment profile prior to drawdown, the existing "Offered" loan should be cancelled on the Web Portal and a new loan application processed.

Once a term loan has been repaid it is "Closed" and cannot be redrawn. Should more funds be required a new facility needs to be applied for. Similarly, should a tranche of a loan be repaid (early or otherwise) it cannot be redrawn – a fresh application needs to be made. Utilisation of invoice finance and overdraft facilities can fluctuate up to the prevailing agreed maximum limit throughout their terms.

6.5 Payment of the EFG Guarantee Premium

6.5.1 Introduction

The EFG Guarantee Premium is the amount of money the Borrower pays to BIS as a contribution towards the costs of Government providing the scheme rather than to cover the cost of the risk.

The scheme is far from self-financing. The availability of the guarantee is deemed to have made the difference between the Borrower not being able to obtain a loan and being able to obtain a loan – i.e. a binary decision. In return for Government providing the means (i.e. the guarantee) for the Lender to say "Yes" to the Borrower when they would have otherwise said "No" the Borrower pays a contribution.

Please note that in July 2011 BBB appointed a new Premium Collection Agency ("PCA") for both the EFG and SFLG schemes. This PCA has put in place a series of systems and processes intended to simplify and automate collection arrangements. As a result, a revised guidance note on these collection arrangements has been circulated to Lenders.

The Guidance Note on Revised Premium Collection Arrangements for SFLG and EFG Schemes (Revised in February 2012) is available in the help section on the Web Portal.

Please also refer to section 5.3.6 and Appendix 9.3 for details on the Premium Payment Schedule.

6.5.2 Premium Value

The Borrower pays 2% p.a. to BIS on the outstanding term loan balance, or the full facility limit for any revolving credit facility. Invoice finance premiums are payable at 2% p.a. but on an industry benchmarked average facility utilisation rate (to reflect the fact the Lender controls the release of funds).

The Premium is payable quarterly in advance by Direct Debit, the amount is set out in the Premium Payment Schedule calculated by the Web Portal and set to the Borrower by the Lender alongside the Scheme Facility Letter. The Schedule sets out the total due and the timing and amount of each quarterly payment.

6.5.3 Payment Arrangements

An independent PCA is contracted to collect all Premiums on behalf of BIS by direct debit. The Direct Debit Mandate is available from the Web Portal.

The first direct debit is collected within a month of draw down (see section 6.5.4 below). It is essential that the Direct Debit Mandate has been completed and signed before draw down takes place. The original signed Direct Debit Mandate is to be sent to the branch of the relationship bank for processing. It is recommended that if the Lender is not the relationship bank that a copy of the Direct Debit Mandate is also kept on file.

Premium Refunds

Guarantee Premiums are collected quarterly in advance and are not reimbursed in the eventuality that the facility is not made available for the full duration of the relevant quarter, i.e. no refunds are available where a facility's duration in months is not divisible by three, or where an early settlement means that the period covered by the quarterly premium will extend beyond the date on which the facility is repaid.

Premium References in DDIs

Lenders commonly use the loan reference number as part of the Direct Debit Mandate reference. BBB have been advised that the direct debit system cannot handle the "+", which forms a part of an EFG reference number, as generated by the Web Portal (e.g.: "24GATHG+01"). It is suggested that the"+01" suffix is dropped when using the loan reference on the Direct Debit Mandate.

6.5.4 Payment Timetable

The first Premium payment

The first Premium payment is made approximately one month following draw down. The current process is as follows:

- Drawdown is made and the Lender sends the original Direct Debit Mandate to the Borrower's bank (which may be the same organisation).
- At the start of each week the PCA runs a report from the EFG Web Portal which advises which facilities have been granted the previous week. The PCA matches the Direct Debit Mandates received to the newly guaranteed facilities on the Web Portal.
- The PCA then verifies the information, and the Premium payment occurs three weeks after the match has been made. Generally, the whole process takes about 4 weeks.

- For example, if a loan is guaranteed on the portal on Monday day 1, the PCA will extract the portal (schedule) information the following week, match the Direct Debit Mandate to the Premium Payment Schedule extract over the following 3 weeks or so, and the Premium is collected at the earliest opportunity – but generally on Tuesday day 30. Initial Premiums are always taken on a Tuesday.

The second Premium payment

The second payment is on the 14th of the month, on the third calendar month following drawdown.

The third and all subsequent payments

The third and all further Premium payments are made on the 14th of the month, exactly 3 months following the previous payment.

Rescheduling facilities

- Lenders notify BIS of the rescheduling of loans via the Web Portal.
- On the first working day of each month the PCA runs a report which details all rescheduled loans. Old reschedules are deleted and new schedules are then established.
- Note that rescheduling is only possible for changes to Premiums in the following month (this is clearly highlighted on the Web Portal).
- For example, if a Lender enters a reschedule on the 2nd of the month for a payment on the 14th of the month, this will not be actioned until the 14th of the following month.

6.5.5 Non-Payment of the Premium

In the event of a Borrower failing to make the direct debit payment:

- If the Borrower fails to make the first Premium payment, the guarantee is not valid. Therefore, it is imperative from the Lender's perspective that this first payment is honoured.

- If a subsequent Premium payment is missed, the Lender (via the designated point of contact for non-payment of Premiums) will be told in writing within 10 business days by the PCA that the Borrower has failed to make a payment. Note that the PCA will contact the Lender on one occasion only to inform of a missed payment.

- When a Premium payment is missed, in order to keep the guarantee active, the Lender can make a Premium payment on behalf of the Borrower and then reclaim the payment from the Borrower. The Premium payment should be paid within twelve weeks of the date the original Premium was due (i.e. before the next quarterly payment is due) or, if the

EFG facility is for 1 year duration or less, the overdue Premium must be paid within 6 weeks.

- If the overdue Premium payment has not been made within this timeframe, the Lender has a further 14 weeks to remedy the situation. Failure by the Lender to act at the 6 month point after the original due date of the guarantee Premium will result in the Government guarantee for the EFG facility automatically expiring.

There is a fundamental principle in the operation of EFG that the provision and continuing validity of the guarantee is conditional on the Premium being paid. The Lender's ability to benefit from the guarantee is dependent upon the Borrower paying the Premium. For this reason the Lender may step in and pay the premium on the Borrowers behalf in order to be certain of the continuity of the Guarantee.

The timeline for making-up any missed Premium payment is a concession intended to assist the Lender rather than a justification for being in arrears (which is contrary to the fundamental principle above). Therefore, there is a requirement to make up the arrears before settlement of a Demand.

6.5.6 Further Notes on Premium Payments

- When a Lender has more than one customer which has missed the Premium payment then technically a separate cheque should be issued for each missed Premium. However, the PCA will accept cheques that aggregate overdue Premiums from more than one Borrower so long as any such payment is accompanied by a list breaking the payment down into the individual amounts. Note however that payments relating to "Legacy SFLG", "New SFLG" and EFG must not be mixed. Separate payments are required for each category of guarantee.

- If the Premiums are not paid, the guarantee lapses after 6 months, and this includes scenarios where the Lender or Borrower has cancelled a direct debit in error. The direct debit should only be cancelled if:
    a. there is a Claim to BIS on the guarantee;
    b. the loan has been repaid early; or
    c. the Lender has decided that the guarantee is no longer appropriate.

- A reconciliation of Premiums actually collected compared with those due to be collected is performed monthly by BBB. This process includes the issuing of exception reports to any Lender for which anomalies have been identified.

6.5.7 Direct Debit Indemnities

It is the Lender's responsibility to ensure that the Premium Schedule is up-to-date. Inaccurate schedules may result in incorrect payments being made under the direct debit system. The Lender must also ensure that the direct debit is cancelled at the end of the loan period.

Where the Borrower pays too much Premium as a result of Premium Schedules being out-of-date, the Borrower will be entitled to raise an indemnity claim against the Lender. The Lender may then enter a dialogue with BBB with regards to any refund.

7 EFG Demands and Recoveries

7.1 Overview

The following table outlines the key stages in the Demands and Recoveries process.

1. Demand on Borrower
2. Pursue Borrower for Repayment / Recovery of Outstanding Exposure
3. Recoveries Procedures (via Security Realisation or Recovery Procedures)
4. Apportion Recovery Proceeds
5. Claim on the Guarantee
6. Subsequent Procedures and Recoveries

A summary of the process, and how it compares to SFLG, is provided in section 7.6.

7.2 Key Stages in the Demands and Recoveries Process

1. Demand on Borrower

- Demand on the Borrower is defined as the date on which the Lender makes Formal Demand in writing to the Borrower for repayment of the outstanding borrowing (this does not include periods of negotiation prior to the Lender issuing Formal Demand).

- The date of Demand on the Borrower must be notified on the EFG Web Portal within 10 business days of the Demand being made.

- The amount entered on the Web Portal should ideally be the total outstanding capital that is owed on the EFG-backed facility, as stated in the Demand Letter. However, if the Lender’s normal practice is to aggregate capital and interest (and in some circumstances, fees) to give a single figure on the Demand Letter, or to aggregate amounts owing on multiple facilities, then this is the figure that should be recorded on the Web Portal at this stage. The key point here is that to assist with any subsequent audit of the facility by the External Auditor, the figure entered on the Web Portal as the Demand on the Borrower ("Lender Demand") must be exactly the same as the Lender Demand figure as stated on the Demand Letter.

- Some smaller lenders do not issue Formal Demand letters to borrowers but instead issue a Letter of Termination. Any such letter should be treated as the Formal Demand on the Borrower for the purposes of the EFG process.

- If it is a Lender's practice to issue their 'Lender Demand' letter prior to stopping all activity on the respective facility/account, allowing a period for the Borrower to enter into dialogue to agree a way forward before the file is passed to recoveries, a second letter should be issued by the recoveries team detailing the balance to be called-in. This should be used as the basis for updating the Web Portal status rather than the letter previously issued.

- Continued payment of the Premium is not required once a Demand has been made on the Borrower.

- Following Demand on the Borrower, the Lender's normal practice in terms of interest charging should continue. For example, if it is the Lender's normal practice to charge default interest following Demand on the Borrower, then it should continue to do so.

- Section 11.3 of the Web Portal Manual v.3 addresses how to record Demand on the Borrower on the Web Portal.

Pursue Borrower for Repayment/Recovery of Outstanding Exposure

Overriding Principles

- **The existence of the EFG guarantee does <u>not</u> reduce the liability of the Borrower in terms of any outstanding indebtedness to the Lender. The Borrower is liable for 100% of the outstanding EFG exposure**. Therefore, Lenders should pursue Borrowers for repayment of all outstanding EFG exposure as per normal recoveries procedures.

- The EFG guarantee is provided to the Lender (not to the Borrower) to provide security cover in the event that the Lender is unable to recover full repayment from the Borrower and is left with an outstanding "bad debt". It should be made clear to the Borrower that the EFG guarantee does not protect the Borrower from liability under the remaining exposure, nor does it "step in" to repay or reduce exposure on behalf of the Borrower.

- Where only EFG exposure exists (as all other Lender exposure has been repaid) and security remains available, the Lender should pursue such security in order to reduce or repay outstanding EFG exposure. The only exception to this rule is if the remaining security relates to a charge over a Principal Private Residence (PPR), which should not be pursued.

3

- Recoveries Procedures (via security realisation or recovery procedures)

Practical Application

1) Realisations from secured (i.e. formally charged) business or personal assets in relation to EFG exposure (i.e. "Linked Collateral"):

Pursue as per normal Lender procedures on repayment and recoveries of charged business or personal assets. This will include:

a. For **unincorporated businesses**, pursue security realisations from charged business or personal assets or from third party security or guarantees. No charge over a PPR can be in place for security in support of an EFG; and,
b. For **limited companies,** pursue security realisations from business or personal assets in relation to Personal Guarantees (if applicable). For example, from debentures, fixed asset charges and mortgages, as well as any other standard business related security.

2) Realisations from secured (i.e. formally charged) business or personal assets in relation to other Lender commercial debt:

- The Lender should follow their normal security realisation procedures in relation to security charged in support of other Lender commercial debt.
- If all Lender commercial debt has been repaid from security proceeds and only EFG debt remains, surplus security proceeds should be used to repay outstanding EFG debt. The only exception to this rule is if the outstanding security proceeds relate to proceeds from the sale of a PPR. In this instance, these funds <u>cannot</u> be used

to repay EFG exposure and should instead be returned to the Borrower (see guidance below on prohibition on proceeds from sale of a PPR for EFG).

3) Recoveries from unsecured business or personal assets / any other unsecured recoveries, including:

- Any repayments (lump sum, ad-hoc or regular repayments) made to the Lender on a voluntary basis by the Borrower;
- Any payments made to the Lender following legal proceedings against the Borrower, including:
    - any bankruptcy or insolvency proceedings (including Individual or Company Voluntary Arrangements); and,
    - The proceeds of enforcement action against the Borrower which the Lender pursues towards recovery of the debt.

4) Recovery procedures against unsecured sole traders and partners and / or Guarantors in relation to EFG exposure:

- It is recognised that Lenders will usually pursue sole traders, partners and guarantors where personal liability exists for outstanding indebtedness.
- Pursue as per normal Lender procedures on recoveries where personal liability of the Borrower exists, including enforcement procedures where to do so is in-line with the Lender's normal practice for recoveries.
- Lenders must observe that EFG rules strictly prohibit the pursuit or application of sale proceeds from a PPR to repay EFG exposure.
- Where a charge over a PPR exists in relation to other Lender exposure, the Lender should pursue funds from the sale of the PPR as per normal procedures BUT in the event that funds are realised from the PPR and other Lender exposure is fully repaid, if a surplus of proceeds remains, this surplus CANNOT be used to reduce any outstanding EFG exposure and the surplus proceeds should be returned to the Borrower.
- It is recognised that this is a distortion of normal commercial practice for Lenders but is a consequence of the prohibition of PPR related funds being used to repay EFG exposure. The EFG Legal Agreement makes it clear that a Lender cannot take into account any funds received, recovered or realised from any PPR when calling upon any guarantee, indemnity or other security provided by an individual as a means of securing the EFG facility.
- In the event that a property is used both as PPR and a business location (such as in a flat above a shop) and there is one single title deed covering both properties, as the property is the Borrower's

PPR then it is "Excluded Residential Security". As such, the Lender cannot call upon it in the course of the security and recoveries process specific to the EFG backed loans. The Lender can pursue such a property in relation to any other Lender exposure.

- A Borrower with personal liability may, in exceptional circumstances, wish to make a voluntary settlement in respect of the outstanding EFG-backed debt from proceeds of a PPR sale. **For the avoidance of doubt, where EFG debt is held, the Lender must confirm to the Borrower that no such payment is permissible under EFG rules.** It is recognised that this is likely to represent a deviation from the Lender's normal realisation and recoveries practice but is in place to reflect the prohibition on acceptance of PPR security (or proceeds arising from sale of a PPR at the recoveries stage).
- In the event that the only asset available to a Borrower with personal liability or Guarantor is a PPR and the only outstanding debt relates to EFG, the Lender would not be expected to pursue the Borrower / Guarantor to bankruptcy.
- Where other Lender debt is also outstanding and the Lender wishes to pursue repayment of this other outstanding debt via a charging order over the PPR and / or bankruptcy proceedings against the individual, the decision whether or not to do so is a matter for the Lender in accordance with their normal practice. However, if action is taken, the outstanding EFG exposure must remain out of scope.

5) Guarantor Settlements

- Where a Guarantor has provided multiple guarantees and makes a single offer to settle all liabilities, recoveries should be split pro rata relative to the **guarantee amounts.** Recoveries should not be split proportional to the balances outstanding as this may not reflect the Guarantor's relative personal liability against each facility as determined at the outset of the facilities.
- Where the balance outstanding on a facility is below the level allocated from the settlement of the guarantees, normal ranking/apportionment rules should be adopted (i.e. the recovery formula should be used).
- **If the customer seeks to preferrentially repay a specific guarantee first, and particularly guarantees given in respect of facilities other than the EFG-backed facilities, this is not acceptable.** The Borrower is 100% liable for all facilities, the EFG guarantee is provided to the Lender and not the Borrower.

6) Individual Voluntary Arrangements

- Where solely EFG debt has been provided to the Borrower, Lenders should not enter into an IVA agreement where it is clear at the outset that dividends payable to the Lender will include funds arising from the sale or re-mortgage of the Borrower's or Guarantor's PPR.
- Where both EFG and non-EFG are present, no 'PPR proceeds' should be allocated against the EFG debt.
- Lenders should seek to obtain a breakdown of the dividend from the Insolvency Practitioner and only accept funds from eligible sources in reduction of the outstanding EFG debt.
- There no distinction between a bankruptcy that has been instigated by the Borrower (or another lender) and one instigated by the Bank.
- If the Lender is a minority creditor and out-voted regarding the structure of the IVA proposal, resulting in inclusion of 'PPR proceeds' within the agreement the Lender should withdraw from the IVA if only EFG debt is present.
- Where non-EFG and EFG debts are present, the Lender must ensure that no 'PPR proceeds' are allocated against the EFG debt, even if this means returning dividends.

7) Use of Debt Collection Agents

- If it is the Lender's normal commercial practice to use the services of a Debt Collection Agent ("DCA") it should continue to do so. The DCA needs to be informed with regards to the prohibition on using PPR proceeds to repay EFG.
- Where separate arrangements are reached by Borrowers' with DCAs to repay each account individually rather than as a single total repayment funds should be distributed in line with the agreement. However, a Lender should not intentionally agreed a repayment structure which would be counter to the priority rankings of the outstanding facilities.

8) Sale of Outstanding Debts to a Third Party

- Note that if a Lender sells any outstanding EFG debt to a DCA or any other third party, the proceeds received should be classed as a recovery and any such proceeds should be used to reduce outstanding EFG exposure.

9) Monies Received in Settlement of PPI Mis-selling

- The Insolvency Service takes the view that if a PPI policy was mis-sold before the date of bankruptcy, any claim relating to the alleged mis-selling of the policy is owned by the Receiver (or Trustee) of the bankruptcy estate and not the individual to whom the policy was sold.
- In this situation settlements should not be used in direct reduction of any outstanding debt, but instead paid to the Receiver.
- If the Borrower is not subject to insolvency proceedings, the Lender's settlement with the Borrower will need to address any issues regarding the utilisation of settlement monies to reduce outstanding debt.

10) Cessation of Recovery Procedures

- The Lender should follow its normal commercial practices in terms of recovery and enforcement procedures. This includes cessation of pursuit of Borrowers where no further repayment is likely or possible, as per normal procedures. To assist audit, a file note should be made noting the commercial justification for the decision not to continue pursuing recovery.

11) Recovery Costs

- Lenders are permitted to deduct from the recovery proceeds all reasonable costs incurred in realising the value of the recovery.

4 • Apportion Recovery Proceeds

Making a recovery from an EFG Borrower may not automatically lead to a recovery to the Scheme. The following steps show how to apportion recoveries in accordance with Schedule 2 of the EFG Legal Agreement:

Step 1 – Categorise Debt

- **Divide the outstanding Lender exposure into EFG Debt and non-EFG Debt ("Commercial Debt").**
- **Where there is Commercial Debt, categorise that debt into either:**
  - **Commercial Debt issued before or simultaneous to the EFG Debt; and / or,**
  - **Commercial Debt issued after the EFG Debt.**

For practical purposes, “Commercial Debt issued simultaneous to the EFG Debt” means where the new Commercial and EFG Debt were issued as part of the same funding package to the Borrower. We would anticipate that the facility letter for each would have the same or very similar date even if drawdown does not occur at the same time. Typically, funding lines will be “marked as available” on or around the same date as the EFG Debt – although BBB reserves its discretion to examine specific cases on an individual basis.

Where Commercial Debt is offered (or existing limits are increased) alongside EFG Debt, it is the net amount of such new or increased facilities which is treated as simultaneous debt for the purposes of the recovery provisions.

Step 2 – Apply Proceeds from EFG Linked Collateral

- “Linked Collateral” is any new security that is specifically listed in the EFG Facility Letter.
- Any recoveries from Linked Collateral must be used to repay EFG Debt first.

Notes / Exceptions

- *Where the Linked Collateral was also granted in connection with the simultaneous provision by the Lender of Commercial Debt, the proceeds from the Linked Collateral may be used to discharge the simultaneous Commercial Debt (but not any prior dated Commercial Debt) in priority to the EFG Debt.*
- *Under such circumstances the priority order will be: 1) Commercial Debt issued simultaneously to the EFG Debt; 2) EFG Debt; and 3) other Commercial Debt.*
- *Where EFG Debt has been fully repaid using Linked Collateral, and there is a surplus, the Lender may apply the surplus to Commercial Debt however it sees fit.*

Step 3 – Apply Priority Rules to Outstanding Debt

- **Apply priority rules to the remaining recovery funds and outstanding debt:**
  - **Where there is only EFG Debt then all of the proceeds will apply to the EFG Debt (where permitted).**
  - **Any Commercial Debt issued prior or simultaneous to the EFG Debt ranks before EFG Debt for receipt of remaining recovery proceeds.**
  - **If prior or simultaneous Commercial Debt has been fully repaid and there remains a surplus of recovery funds, this surplus should be split (pro-rata) between any remaining EFG Debt and any Commercial Debt issued after the EFG Debt.**
  - **To undertake this pro-rata split of the remaining recovery funds, use the Recovery Formula**

$$\left(\frac{A}{A+B}\right) \times C$$

Where:

- A is the current outstanding value of EFG Debt
- B is the current outstanding value of Commercial Debt
- C is the value of remaining recovery funds available
- Deduct the appropriate proportion of remaining recovery funds from the outstanding EFG balance to give a reduced outstanding EFG balance.

Notes / Exceptions

- *PPR funds (whether arising through the enforcement of security or otherwise) are never permitted to be applied to an EFG Debt.*
- *For the avoidance of doubt, having realised funds attributable to a PPR and applied it to Commercial Debt, any surplus proceeds thereafter should be returned to the owner of the PPR and not applied to EFG Debt.*
- *Where a Lender is applying recoveries from a) PPR and b) other (non-PPR) assets to Commercial Debt, Lenders must follow their normal procedures in relation to the order of application of the PPR and the non-PPR assets.*
- *If there is Commercial Debt that a) is backed by a specific legal charge (for example, a chattels mortgage); and b) the charge does not include an "all monies and liabilities" clause then, in such circumstances, the related Commercial Debt should be repaid in the first instance with any surplus monies thereafter, if any exist, to go to the Borrower.*
- *Where the Borrower has a prior (to EFG debt) overdraft then the value of the "prior debt" is up to a maximum of the overdraft limit at the time that the EFG was offered. If at default, the balance on the overdraft is higher than the limit (prior to EFG being granted) and / or the overdraft limit has been subsequently increased, then this additional overdraft balance (or limit, if limit has been increased) ranks on an equal basis to EFG debt in terms of priority for receipt of recovery proceeds. All overdraft exposure up to the original overdraft limit (when EFG facility was granted) has priority over EFG for receipt of recovery proceeds.*

5

- Claim on the Guarantee

The EFG provides the Lender with a guarantee equivalent to 75% of the outstanding value of any individual facility, after recovery proceeds have been applied (the "Guarantee Rate"), subject to the Annual Claim Limit.

Process

- The Lender should make each Claim on the Guarantee individually on the EFG Web Portal. Note that the value recorded on the EFG Web Portal should be 100% of the outstanding EFG balance (after application of recovery proceeds if appropriate) and should not be reduced to reflect the

75% of the EFG guarantee at this stage, as the EFG Web Portal automatically applies the 75% to the figure entered.

- The Claim on the Guarantee should not include any interest that has accrued and which is outstanding on the EFG facility (save where the EFG facility is either an eligible overdraft or invoice finance / factoring facility in which case interest which has accrued prior to the earlier of the date on which the Lender makes Demand for repayment on the Borrower and the scheduled expiry date of the facility may be included).

- Where a defaulting EFG-backed facility has any form of Business Loan Repayment Insurance ("BLRI") the use of BLRI proceeds in reduction of the outstanding balance should be undertaken where the policy is directly linked to the EFG facility and the Lender has a clear entitlement to the proceeds, possibly through an assignment of the BLRI policy or being named as the beneficiary of the policy.

- Where the Borrower is insolvent, the Lender has not formally assigned a policy and the Borrower is named as the beneficiary, the Lender may not have an automatic right to use proceeds from any claim in reduction of the outstanding balance and any monies received could be payable to the receiver.

- Any cancellation costs or other charges relating to the insurance cannot be added to the amount of the Claim.

- If the Lender chooses to place recovery funds from Linked Collateral in a suspension or impersonal account prior to making a Claim on the Guarantee, such recoveries should not be applied to the outstanding balance of an EFG facility before making a Claim. When such funds are subsequently released, they should be treated as any other post-claim recovery (as described in Step 6 below).

- When a debt restructure is agreed between the Lender and the Borrower, a Claim may be made where, following demand on the Borrower, any potential restructuring would not be expected to result in repayment of all (or significantly all) of the outstanding amount. A Claim can also be made once a debt has been restructured for the full outstanding amount but the Borrower subsequently defaults and demand is, again, made on the Borrower.

- Where the restructuring is a change to the repayment profile but not the total anticipated repayment, then the loan should continue as normal. The EFG Web Portal should be used to reflect any changes in the structure of the debt (using the "Change Amount or Terms" screen). If a restructure follows Demand on the Borrower, and the total anticipated repayment is for the full outstanding amount, then the status of the facility should be changed back to "Guaranteed".

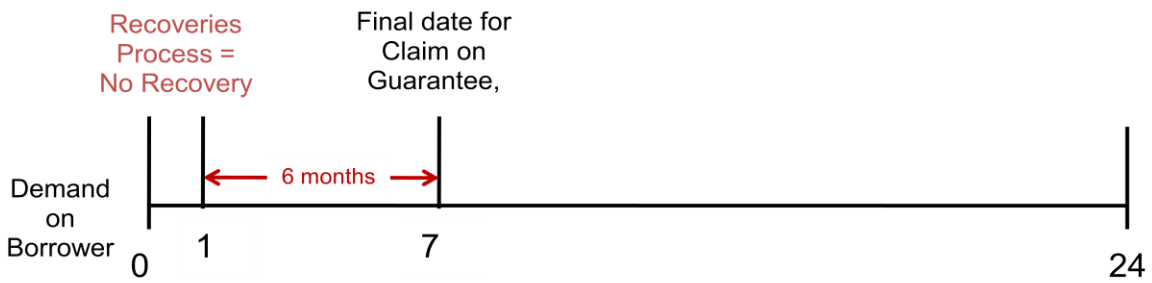
- If the Lender believes that a full repayment of the outstanding amount is less certain than originally envisaged, but still realistically possible, a Claim should not be made. However, a Claim may be made if the Lender does not believe that the Borrower has the capacity to fully repay the debt under the original or restructured terms – as evidenced by normal commercial procedures.

Timing Rules for Making a Guarantee Claim

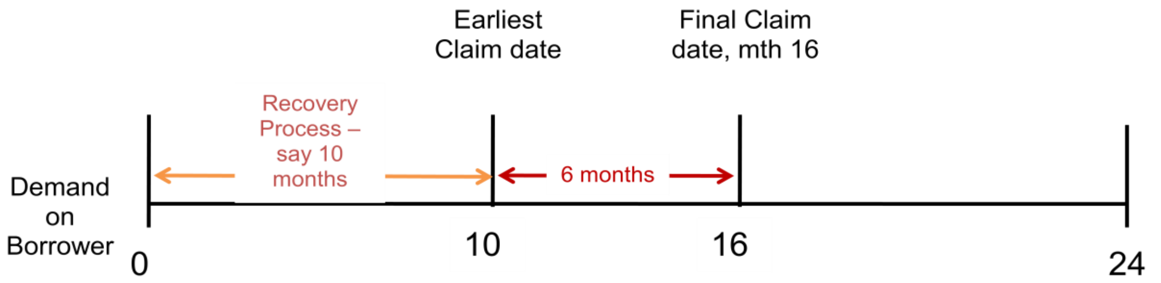
- A Claim on the Guarantee must be made within 6 months of completion of the recovery process or 24 months of Lender Demand, whichever is the sooner.

- Note that a Claim on the Guarantee is not to be a substitute for normal recovery procedures. Where no security is available a Lender should follow its normal recoveries processes, and may then make a Claim on the Guarantee. The value of the Claim on the Guarantee may differ to the value of the Demand on the Borrower, which may include interest payments and fees. Moreover, capital repayments may have been received in the intervening period.

- In the following example the Lender has attempted recovery for one month before stopping (and has made a note of the commercial justification for ceasing the process). The Lender then has a further 6 months in which to make a Claim on the Guarantee.



- In the following example, the Lender attempts recovery for 10 months, records the termination of the recovery effort, and can, therefore, make a claim any time before 16 months.



- Where the recovery process remains incomplete 18 months after Formal Demand has been made on the Borrower by the Lender, then the Lender can, at this point, make a claim to BIS for 75% of the outstanding principal amount of the EFG balance.

- Although a Claim is made at this point, the Lender is expected to continue their recovery procedures thereafter (subject to normal commercial practice).

Demand Invoice

- The Demand Invoice is the document via which the Lender formally seeks payment from BBB for all of the Claims on the Guarantee which have been recorded on the Web Portal during the preceding quarter.

- Claims may be made on a quarterly basis, on quarters ending 31st March, 30th June, 30th September and 31st December. To make a claim, Lenders must forward a hard copy of the Demand Invoice (and Recoveries Statement, where applicable) to BBB at the end of the quarter reflecting activity recorded on the Web Portal over the period.

- Each Demand Invoice should be presented on the Lender's letterhead or other official stationery and should contain the following information:
  - The date on which it is being submitted
  - A unique reference number assigned by the Lender
  - The period / quarter to which it refers
  - A name and contact details for queries
  - For each facility against which Demand is being made:
    - the loan reference number
    - the business name

    - the amount being claimed
- The total number and value of the Demands listed on the invoice

- Only one Demand Invoice may be submitted for each quarter and should be submitted as soon as possible after the end of the quarter to which it refers. Any EFG facilities omitted from a Demand Invoice in error should be included on the following quarter's Demand Invoice.

- The maximum amount claimable in respect of those EFG facilities offered in any one scheme period is the Annual Claim Limit for the Lender in respect of that period.

Settlement of Demand

- BBB will advise the Lender of the settlement of each individual EFG facility by changing the status of the loan record on the Web Portal from "Demand against Guarantee" to "Settled".

- BBB will make payment to the Lender within 30 days of receipt of the Demand Invoice. Demands and Recoveries are "netted off" each quarter by the Lender and BIS will make a payment within 30 days to the Lender for the net amount. In the event that recoveries are higher than claims in any one quarter, the Lender should send a cheque for the difference, payable to "BIS".

Web Portal

- Section 13.4 of the Web Portal Manual v.3 addresses how to record Claims on the Guarantee on the Web Portal.

- The Web Portal enables each Lender to access details of their on-going utilisation of their Annual Claim Limit in respect of any annual scheme period.

6 • Subsequent Procedures and recoveries

Further Recoveries

- Once a Claim on the Guarantee has been made the Lender is still obliged to be mindful of further potential recoveries. Whilst there is no backstop date for recoveries to be made, Lenders should apply their normal commercial judgement to decide when it is appropriate to cease recovery activity.

- If further recoveries are made after settlement of the Claim, Lenders should apply the same apportioning rules as described in Steps 2 and 3 above.

- For recoveries made subsequent to the Guarantee Claim, the following Recovery Formula should be used:

$$\left(\frac{A}{A+B} \right) \times C \times 75\%$$

Where

  - A is the outstanding value of EFG Debt at the time of the Guarantee Claim
  - B is the current outstanding value of Commercial Debt
  - C is the value of remaining recovery funds
  - The resulting balance from the Recovery Formula is the amount due to BIS as a recovery refund

- Note: Any interest (on Commercial Debt and EFG Debt) accrued after a Claim has been made on the EFG guarantee, CANNOT be deducted from any subsequent recovery proceeds.

- If, after applying these apportioning rules, a refund is due to the Secretary of State, this recovery amount should be included on the next Recoveries Statement.

Regular Recovery Plans

- It is recognised that there will be situations where repayment programmes may involve very small monthly repayments. To help reduce administration, where small regular payments are concerned, it is not necessary to update the Web Portal monthly and make quarterly submissions in the Recoveries Statement. Instead, repayments may be aggregated together for submission with less frequency, but preferably at least once per year.

Recoveries Statement

- The “Managing Recoveries” screen within the Web Portal will assist in calculating the correct amount due to the Secretary of State. Repayment details should be recorded on the Web Portal for each EFG facility and, then, on a quarterly basis, repayments across the Lender’s whole portfolio should be entered onto the Recoveries Statement.

- The Recoveries Statement is the document on which the Lender summarises the amounts due to the Secretary of State arising from any recoveries arising from previously settled Demands and accompanies payment of those Recoveries to the Secretary of State.

- Each Recoveries Statement should be presented on the Lender's letterhead or other official stationery and should contain the following information:
    - The date on which it is being submitted;
    - A unique reference number or other identifier assigned by the Lender;
    - The quarter to which it refers; and,
    - A name and contact details for queries.

- For each EFG facility against which a recovery has been made and payment is due to the Secretary of State:
    - the loan reference number;
    - the business name; and,
    - the amount recovered.

- The information on the Recoveries Statement should be consistent with the information already entered on the EFG Web Portal in connection with the facilities affected. The total number and value of the recoveries should be listed on the Recoveries Statement.

- Only one Recoveries Statement may be submitted for each quarter and should be submitted as soon as possible after the end of the quarter to which it refers. Any EFG facilities omitted from a Recoveries Statement in error should be included on the following quarter's Recoveries Statement.

- Please note that more than one recovery can be made per EFG facility.

- In transactional terms funds recovered are netted off from the value of Demands for which settlement is required.

- Following any recovery, update the Web Portal status to "Recovered". BBB will then update the Web Portal status to "Realised".

Incorrect Calculations and Losses

- If the Lender claims the incorrect amount of money under the EFG guarantee then the Lender must repay the money as soon as reasonably practical if it has received an overpayment.

- If the Lender did not claim enough money because of an administrative mistake, the scheme will pay the full amount due as soon as reasonably practical.

- The scheme cannot be held responsible for any other loss or disadvantage the Lender may suffer as a result of being a member of the scheme.

Post Claim Limit Recoveries

- This process becomes effective for a Phase once the Claim Limit has been exhausted.

- The concept of a "post-Claim Limit Realisation" has been introduced as a way of minimising what could otherwise become burdensome administrative implications of dealing with a post-Settlement Recovery.

- Guidance to Lenders is as follows:
  1) Lenders should continue to enter all Claims and Recoveries onto the Portal in the normal way.
  2) Lenders should continue to submit Demand Invoices and Recovery Statements, each broken down by Phase.
  3) Any Demands arising from a Phase for which the Claim Limit has been exhausted will be Settled at nil.
  4) Any Recoveries arising from a Phase for which the Claim Limit has been exhausted will be recorded as post-Claim Limit Realisations. These Recoveries should be excluded from any netting-off between Demand Invoices and Recovery Statements.
  5) The Lender may retain the post-Claim Limit Realisations and assign them to any loans for which Claims within the Phase which have previously been Settled at nil or partially Settled. If the amount of a recovery is greater than any claims that have been Settled as zero for a Phase then these should be returned to BIS. The Lender should maintain a record of the post-Claim Limit Realisations received and the loans in respect of which they have been apportioned.
  6) If there is a situation where an amount is recovered after all claims for a Phase have been settled, the amount received will be due to BIS and be added to the recovery statement as a genuine recovery i.e. NOT as a post claim limit recovery.

7.3 Worked Examples of EFG Default Scenarios

7.3.1 Recovery before a Claim on the Guarantee

SCENARIO ONE

Outstanding EFG Debt (capital only) at default:

- £20,000

Outstanding Commercial Debt at default:

- £60,000 term loan issued at **same time** as the EFG Debt

Security held and funds subsequently realised by the Lender:

- Charge over machinery (all monies) in relation to the term loan – which is sold for £40,000 before the Lender makes a Claim on the Guarantee

Step 1 – Categorise Debt

- EFG Debt exposure is £20,000
- Commercial Debt exposure is £60,000, which is simultaneous debt

Step 2 – Apply proceeds from Linked Collateral

- Not applicable

Step 3 – Apply Priority Rules to Outstanding Debt

- £40,000 is realised from the charge over machinery
- This is used by the Lender to repay the Commercial Debt term loan, leaving £20,000 of Commercial Debt remaining

Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £20,000 = £15,000

Step 5 - Apply Recoveries following a Claim on the Guarantee

- Not applicable

Summary		
Outstanding Commercial Debt	£20,000	(£60,000 - £40,000 recovery)
Outstanding Lender EFG Debt	£5,000	(£20,000 - £15,000 guarantee payment)
Government guarantee paid	£15,000	
	£40,000	

SCENARIO TWO

Outstanding EFG Debt (capital only) at default:

- £20,000

Outstanding Commercial Debt at default:

- £60,000 term loan issued **before** the EFG Debt

Security held and funds subsequently realised by the Lender:

- Charge over machinery (all monies) in relation to the term loan – which is sold for £70,000 before the Lender makes a Claim on the Guarantee
- The Borrower also volunteers to release £10,000 of equity in his house to help pay any outstanding debt

Step 1 – Categorise Debt

- EFG Debt exposure is £20,000
- Commercial Debt exposure is £60,000, which is debt issued before the EFG

Step 2 – Apply proceeds from Linked Collateral

- Not applicable

Step 3 – Apply Priority Rules to Outstanding Debt

- £70,000 is realised from the charge over machinery
- This is used by the Lender to fully repay the Commercial Debt term loan, leaving £10,000 of surplus funds
- The £10,000 is applied to the £20,000 EFG loan, leaving £10,000 EFG exposure
- **Although the Borrower has offered to release equity in his home (PPR), any such funds cannot be applied to EFG debt, and the offer must be declined**

Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £10,000 = £7,500

Step 5 – Apply Recoveries following a Claim on the Guarantee

- Not applicable

Summary		
Outstanding Commercial Debt	£0	(£60,000 - £60,000 recovery)
Outstanding Lender EFG Debt	£2,500	(£20,000 - £10,000 recovery - £7,500 guarantee payment)
Government guarantee paid	£7,500	
	£10,000	

SCENARIO THREE

Outstanding EFG Debt (capital only) at default:
- £20,000

Outstanding Commercial Debt at default:
- £60,000 term loan issued **before** the EFG Debt

Security held and funds subsequently realised by the Lender:
- Charge over machinery (all monies) in relation to the term loan – which is sold for £50,000 before the Lender makes a Claim on the Guarantee
- Personal Guarantee in support of the EFG for £20,000 (Linked Collateral), which is realised before the Claim on the Guarantee

Step 1 – Categorise Debt

- EFG exposure is £20,000
- Commercial Debt exposure is £60,000, which was issued before the EFG

Step 2 – Apply proceeds from Linked Collateral

- The £20,000 Personal Guarantee is applied to the EFG, fully extinguishing the EFG exposure

Step 3 – Apply Priority Rules to Outstanding Debt

- £50,000 is realised from the charge over machinery
- This is used by the Lender to repay the Commercial Debt term loan of £60,000, leaving £10,000 outstanding exposure

Step 4 – Claim on the Guarantee

- There can be no Claim on the Guarantee as the EFG has been fully repaid by the Linked Collateral
- Total loss to the Lender is:
  - £10,000 on the Commercial Debt

Step 5 – Apply Recoveries following a Claim on the Guarantee

- Not applicable

Summary		
Outstanding Commercial Debt	£10,000	(£60,000 - £50,000 recovery)
Outstanding Lender EFG Debt	£0	(£20,000 - £20,000 recovery)
Government guarantee paid	£0	
	£10,000	

SCENARIO FOUR

Outstanding EFG Debt (capital only) at default:

- £20,000

Outstanding Commercial Debt at default:

- £60,000 term loan issued **before** the EFG Debt

Security held and funds subsequently realised by the Lender:

- The Commercial Debt is supported by a charge (all monies) over commercial property. A recovery is made on the commercial property, realising £40,000
- A Personal Guarantee for £30,000 was also in place in support of the Commercial Debt (all monies). A recovery has been made from the Personal Guarantee for £30,000, deriving from sale proceeds from a Principal Private Residence

Step 1 – Categorise Debt

- EFG exposure is £20,000
- Commercial Debt exposure is £60,000, which was issued before the EFG

Step 2 – Apply proceeds from Linked Collateral

- Not applicable

Step 3 – Apply Priority Rules to Outstanding Debt

- £40,000 is realised from the charge over commercial property. This is used by the Lender to repay the Commercial Debt term loan of £60,000, leaving £20,000 exposure
- £30,000 is realised from PPR. £20,000 of this is used to fully repay the outstanding exposure on the Commercial Debt
- The £10,000 remaining recovery may not be applied to the EFG and must be returned to the Borrower

Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £20,000 = £15,000

Step 5 – Apply Recoveries following a Claim on the Guarantee

- Not applicable

Summary		
Outstanding Commercial Debt	£0	(£60,000 - £40,000 recovery - £20,000 PPR recovery)
Outstanding Lender EFG Debt	£5,000	(£20,000 - £15,000 guarantee payment)
Government guarantee paid	£15,000	
	£20,000	
Note: In the above example, if the £30,000 PPR recovery is applied before the £40,000 machinery recovery, then there would be no return of funds to the Borrower. It is envisaged that Lenders would normally apply non-PPR recoveries before a PPR recovery. The Lender must apply its normal commercial practice, but where PPR recoveries are applied first, the use of such policy should be recorded in file notes.		

SCENARIO FIVE

Outstanding EFG Debt (capital only) at default: £20,000

Outstanding Commercial Debt at default:
- £30,000 term loan issued after the EFG Debt

Security held and funds subsequently realised by the Lender:
- Charge over property (all monies) in relation to the Commercial Debt – which is sold for £40,000 before the Lender makes a Claim on the Guarantee

Step 1 – Categorise Debt

- EFG Debt exposure is £20,000
- Commercial Debt exposure is £30,000, which was issued after the EFG

Step 2 – Apply proceeds from Linked Collateral

- Not applicable

Step 3 – Apply Priority Rules to Outstanding Debt

- £40,000 is realised from the charge over the property
- As the Commercial Debt was issued after the EFG Debt it has equal (pro-rata) priority to the EFG Debt for receipt of recovery funds
- The £40,000 is therefore applied pro-rata to the EFG Debt as follows:
  - ((A)/(A+B)) x C = ((20,000)/(20,000 + 30,000)) x £40,000 = £16,000
  - £20,000 outstanding EFG Debt less £16,000 leaves £4,000 outstanding on the EFG Debt
  - Repayment towards Commercial Debt is £24,000 (£40,000 - £16,000). Applying this £24,000 to the £30,000 Commercial Debt leaves £6,000 outstanding)

Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £4,000 = £3,000

Step 5 – Apply Recoveries following a Claim on the Guarantee

- Not applicable

Summary		
Outstanding Commercial Debt	£6,000	(£30,000 - £24,000 recovery)
Outstanding Lender EFG Debt	£1,000	(£20,000 - £16,000 recovery - £3,000 guarantee payment)
Government guarantee paid	£3,000	
	£10,000	

7.3.2 Recovery after a Claim on the Guarantee

SCENARIO ONE

Outstanding EFG Debt (capital only) at default:
- £20,000

Outstanding Commercial Debt at default:
- £60,000 term loan issued **before** the EFG Debt

Security held and funds subsequently realised by the Lender:
- Charge over property (all monies) in relation to the Commercial Debt – which is sold for £70,000 after the Lender makes a Claim on the Guarantee

Step 1 – Categorise Debt

- EFG exposure is £20,000
- Commercial Debt exposure is £60,000, which was issued before the EFG

Steps 2 – 3

- Not applicable – no recovery before the Claim

Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £20,000 = £15,000

Summary so far		
Outstanding Commercial Debt	£60,000	
Outstanding Lender EFG Debt	£5,000	(£20,000 - £15,000 guarantee payment)
Government guarantee paid	£15,000	
	£80,000	

Step 5 – Apply Recoveries following a Claim on the Guarantee

Revisit Steps 2 – 3: Not applicable – there is no PPR or Linked Collateral

Revisit Step 4 – Apply Priority Rules to Outstanding Debt

- £70,000 is realised from the charge over the property
- This is used by the Lender to fully repay the Commercial Debt term loan of £60,000, leaving £10,000 surplus recovery funds which can be used to reduce outstanding EFG Debt
- Of this £10,000, 75% needs to be refunded back to the scheme as its share of the recovery proceeds. To calculate the amount to be repaid to the scheme, calculate 75% of surplus recovery funds (i.e. £10,000 x 75%)
- £7,500 is, therefore, to be refunded to the scheme (the refund must always be lower than the amount claimed under the guarantee)

- The remaining £2,500 can be used by the Lender to reduce its outstanding EFG exposure

Summary		
Outstanding Commercial Debt	£0	(£60,000 - £60,000 recovery)
Outstanding Lender EFG Debt	£2,500	(£20,000 - £15,000 guarantee payment - £2,500 recovery)
Government guarantee paid	£7,500	(£15,000 - £7,500 refund)
	£10,000	

SCENARIO TWO

Outstanding EFG Debt (capital only) at default: • £20,000 Outstanding Commercial Debt at default: • £60,000 term loan issued **after** the EFG Debt Security held and funds subsequently realised by the Lender: • Charge over property (all monies) in relation to the Commercial Debt – which is sold for £50,000 after the Lender makes a Claim on the Guarantee.

Step 1 – Categorise Debt

- EFG exposure is £20,000
- Commercial Debt exposure is £60,000, which was issued after the EFG

Steps 2 – 3

- Not applicable – no recovery before the Claim

Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £20,000 = £15,000

Summary so far		
Outstanding Commercial Debt	£60,000	
Outstanding Lender EFG Debt	£5,000	(£20,000 - £15,000 guarantee payment)
Government guarantee paid	£15,000	
	£80,000	

Step 5 – Apply Recoveries following a Claim on the Guarantee

Revisit Steps 2 – 3: Not applicable – there is no PPR or Linked Collateral

Revisit Step 4 – Apply Priority Rules to Outstanding Debt

- £50,000 is realised from the charge over the property
- As the Commercial Debt was issued after the EFG it has equal (pro-rata) priority to the EFG Debt for receipt of recovery funds
- Of the £50,000 the amount repayable to the Secretary of State is calculated as follows:
    - ((A)/(A+B)) x C = ((20,000)/(20,000 + 60,000)) x £50,000 = £12,500
    - £12,500 x 75% = £9,375
    - The final guarantee settlement is therefore the original claim of £15,000 less refund of £9,375 = £5,625
    - The Lender can keep the remaining recovery funds (25% x £12,500 = £3,125) and apply it to its outstanding EFG Debt

- In addition, the Lender can also apply the outstanding balance of recovery funds (£50,000 - £12,500 = £37,500) towards repayment of its outstanding Commercial Debt

Summary		
Outstanding Commercial Debt	£22,500	(£60,000 - £37,500 recovery)
Outstanding Lender EFG Debt	£1,875	(£20,000 - £15,000 guarantee payment - £3,125 recovery)
Government guarantee paid	£5,625	(£15,000 - £9,375 refund)
	£30,000	

SCENARIO THREE

Outstanding EFG Debt (capital only) at default:

- £110,000 (against limit of £150,000)

Outstanding Commercial Debt at default:

- An overdraft provided prior to the EFG facility with outstanding balance of £10,000
- A term loan provided subsequent to the EFG facility with outstanding balance of £30,000

Security held and funds subsequently realised by the Lender:

- Charge over machinery (all monies) which is sold for £40,000 after the Lender makes a Claim on the Guarantee

Step 1 – Categorise debt

- EFG Debt exposure is £110,000
- Commercial Debt exposure is £40,000
    - £10,000 of which is prior debt
    - £30,000 is subsequent debt

Steps 2 – 3: Not applicable – the recovery is not made until after the Claim on the Guarantee

Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £110,000 = £82,500

Summary so far		
Outstanding Commercial Debt	£40,000	
Outstanding Lender EFG Debt	£27,500	(£110,000 - £82,500 guarantee payment)
Government guarantee paid	£82,500	
	£150,000	

Step 5 – Apply Recoveries following a Claim on the Guarantee

Revisit Step 2: Not applicable – there is no Linked Collateral

Revisit Step 3 – Apply Priority Rules to Outstanding Debt

- Following the claim under the Guarantee, £40,000 is realised from the charge over machinery.
- This is used by the Lender to repay in full the outstanding overdraft of £10,000 leaving a surplus of £30,000

- Out of the surplus of £30,000 an amount is repayable to the Secretary of State – calculated as follows :
    - ((A)/(A+B)) x C= ((110,000)/(110,000 + 30,000)) x £30,000 = £23,571
    - £23,571 x 75% = £17,679
    - Refund payable to the Secretary of State = £17,679
    - The Lender can keep the remaining recovery funds (25% of the £23,571 = £5,892) and apply it to its outstanding EFG Debt

- The Lender can apply the balance of £6,429 (£30,000 - £23,571) towards repayment of the Commercial Debt term loan.

Summary		
Outstanding Commercial Debt	£23,571	(£40,000 - £10,000 recovery - £6,429 recovery)
Outstanding Lender EFG Debt	£21,608	(£110,000 - £82,500 guarantee payment - £5,892 recovery)
Government guarantee paid	£64,821	(£82,500 - £17,679 refund)
	£110,000	

7.3.3 Recovery before and after a Claim on the Guarantee

SCENARIO ONE

Outstanding EFG Debt (capital only) at default:

- £110,000 (against limit of £150,000)

Outstanding Commercial Debt at default:

- An overdraft provided prior to the EFG facility with outstanding balance of £30,000
- A commercial mortgage which was provided after the EFG facility with outstanding balance of £250,000

Security held and funds subsequently realised by the Lender:

- Charge over machinery (all monies) which is sold for £40,000 before the Lender makes a Claim on the Guarantee
- A charge over a factory building to which the commercial mortgage relates (all monies) which is sold for £275,000 after the Lender makes a Claim on the Guarantee
- A Personal Guarantee for £50,000 (taken when the EFG facility was provided) provided by the Managing Director of the business through which £40,000 is obtained (after the Lender makes Claim on the Guarantee)

Step 1 – Categorise Debt

- EFG Debt exposure is £110,000
- Commercial Debt exposure is £280,000:
    - £30,000 on overdraft (prior debt)
    - £250,000 relating to a commercial mortgage (subsequent debt)

Step 2 – Apply proceeds from Linked Collateral

- Not applicable

Step 3 – Apply Priority Rules to Outstanding Debt

- The Lender applies the £40,000 realisation from the charge over machinery to repay in full the overdraft leaving a surplus of £10,000
- This surplus then needs to be applied pro-rata to the outstanding EFG Debt and Commercial Debt and is calculated as follows:
    - ((A)/(A+B)) x C = ((110,000)/(110,000 + 250,000)) x £10,000 = £3,060 (leaving £106,940 outstanding on the EFG Debt)
    - Repayment towards Commercial Debt = £10,000 - £3,060 = £6,940 (the Lender uses this towards repayment of the commercial mortgage: £250,000 - £6,940 = £243,060)

Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £106,940= £80,205

Summary so far		
Outstanding Commercial Debt	£243,060	(£280,000 - £30,000 recovery - £6,940 recovery)
Outstanding Lender EFG Debt	£26,735	(£110,000 - £3,060 recovery - £80,205 guarantee payment)
Government guarantee paid	£80,205	
	£350,000	

Step 5 – Apply Recoveries following a Claim on the Guarantee

Revisit Step 2 – Apply proceeds from PPR – not applicable

Revisit Step 2 – Apply proceeds from Linked Collateral

- The Personal Guarantee is Linked Collateral – therefore, 75% of £40,000 = £30,000 must be repaid to the Secretary of State and the remaining £10,000 can be retained by the Lender and applied to the EFG Debt
- Resulting EFG Debt is therefore £26,735 - £10,000 = £16,735 and resulting guarantee claim is £80,205 - £30,000 = £50,205

Revisit Step 3 – Apply Priority Rules to Outstanding Debt

- All of the £275,000 recovery from the charge over the factory building is to be apportioned between the EFG Debt and the Commercial Debt (as there remains no outstanding prior Commercial Debt against which it can be applied, the overdraft having already been repaid in full)
- Out of the surplus of £275,000 the amount repayable to the Secretary of State is calculated as follows:
- The amount owing on the EFG Debt in total is:
    - The guarantee (as paid earlier) £80,205
    - Less the recovery from the Linked Collateral (£30,000)
    - Plus the outstanding Lender EFG Debt <u>£16,735</u>
    - =A (in the formula) £66,940

    - ((A)/(A+B)) x C= ((66,940)/(£66,940 + 243,060)) x £275,000 = £59,382
    - 75% is repaid to the Secretary of State: 75% x £59,382 = £44,536 (the final guarantee balance is £50,205 - £44,536 = £5,669)
    - 25% is retained by the Lender: 25% x £59,382 = £14,845. This can be used to repay outstanding EFG Debt: £16,735 - £14,845 = £1,890

- The balance of recovery monies from the sale of the commercial property of £215,618 (£275,000 - £59,382) can be paid towards repayment the commercial mortgage:
    - £243,060 - £215,618 = £27,442

Summary		
Outstanding Commercial Debt	£27,442	(£243,060 as above - £215,618 recovery)
Outstanding Lender EFG Debt	£1,890	(£26,735 as above – 10,000 recovery - £14,845 recovery)
Government guarantee paid *	£5,668	
	£35,000	
*Original claim of £80,205, less repayment from the Personal Guarantee of £30,000, less repayment from the commercial property of £44,536.		

Checking the Above

The net result should be the same, whether recoveries are made before or after a Claim on the Guarantee. A way of checking complex claims after the guarantee is to calculate the same, as if all claims are made before the Claim on the Guarantee. This is demonstrated below using the above example.

Step 1 – Categorise Debt

- EFG Debt exposure is £110,000
- Commercial Debt exposure is £280,000:
  - £30,000 on overdraft (prior debt)
  - £250,000 relating to a commercial mortgage (subsequent debt)

Step 2 – Apply proceeds from Linked Collateral

- Apply the £40,000 Personal Guarantee to the £110,00 EFG Debt, leaving EFG Debt of £70,000

Step 3 – Apply Priority Rules to Outstanding Debt

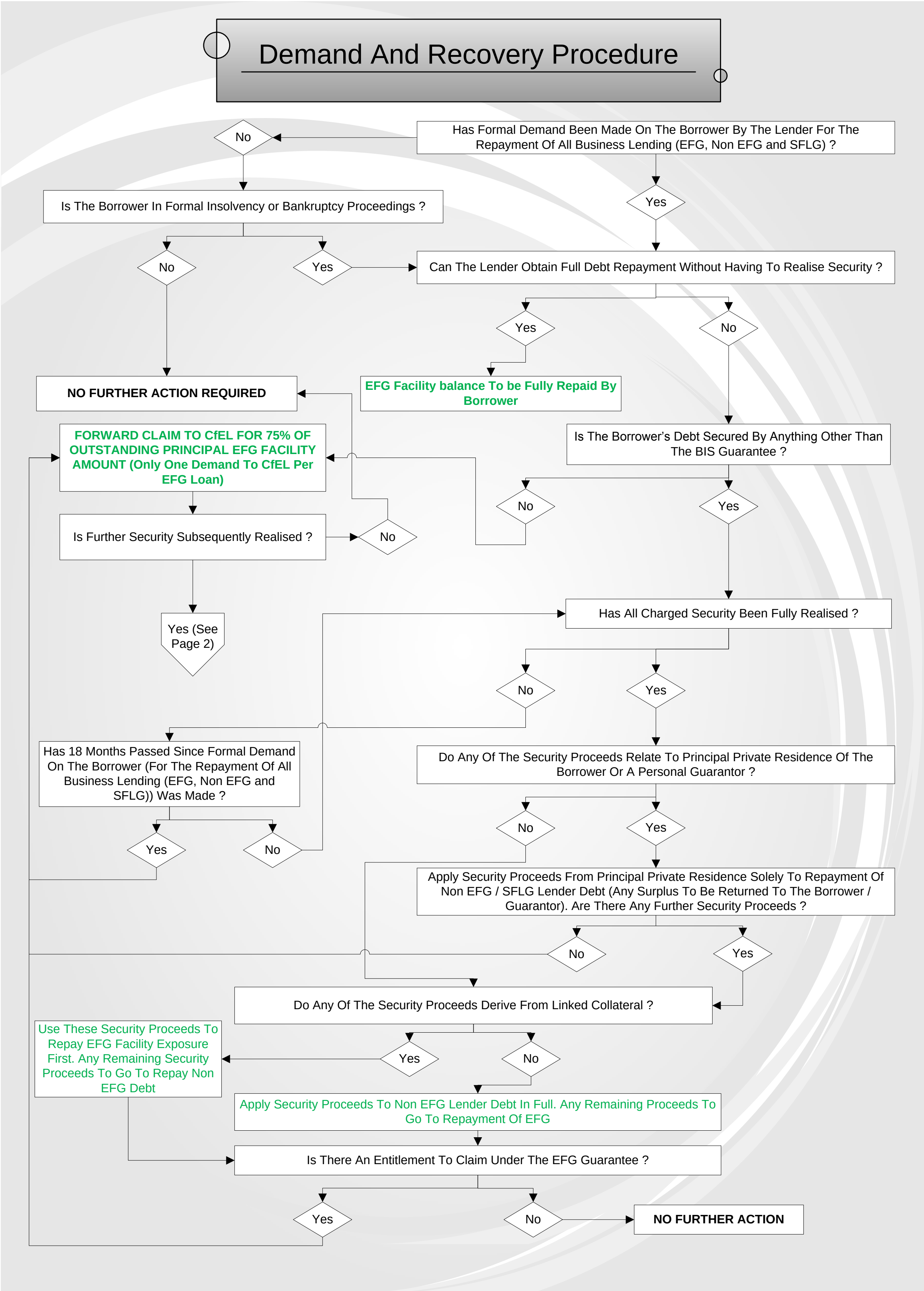
- The Lender applies the £40,000 realisation from the charge over machinery to repay in full the overdraft leaving a surplus of £10,000
- This is added to the £275,000 recovery on the commercial mortgage, giving £285,000 surplus
- This surplus then needs to be applied pro-rata to the EFG Debt calculated as follows:
  - ((A)/(A+B)) x C= ((70,000)/(70,000 + 250,000)) x £285,000 = £62,344
  - EFG Debt of £70,000 less £62,344 gives £7,656 outstanding
  - Repayment towards Commercial Debt = £285,000 - £62,344 = £222,656.
  - Commercial Debt of £250,000 less £222,656 = £27,344

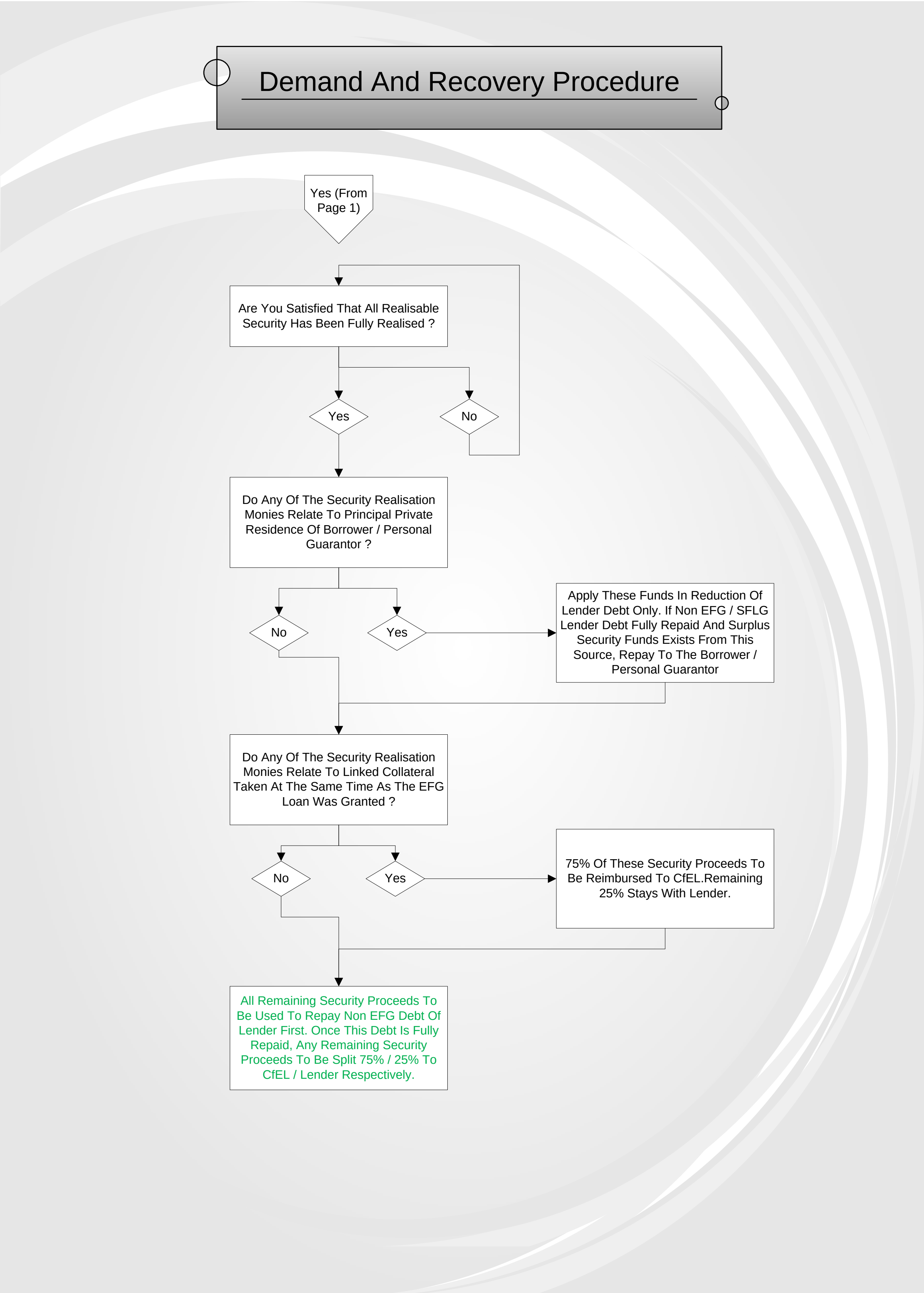
Step 4 – Claim on the Guarantee

- Lender is entitled to claim 75% x £7,656 = £5,742
- Outstanding EFG Debt is £7,656 less £5,742 = £1,914

Summary *(some differences due to rounding)*		
Outstanding Commercial Debt	£27,344	(£280,000 - £30,000 recovery - £222,656 recovery)
Outstanding Lender EFG Debt	£1,914	(£110,000 - £40,000 recovery - £62,344 recovery - £5,742 guarantee payment)
Government guarantee paid	£5,742	
	£35,000	

7.4 Demands & Recovery Procedure – Flowchart




Demand And Recovery Procedure
Yes (From Page 1)
Are You Satisfied That All Realisable Security Has Been Fully Realised ?
Yes
No
Do Any Of The Security Realisation Monies Relate To Principal Private Residence Of Borrower / Personal Guarantor ?
No
Yes
Apply These Funds In Reduction Of Lender Debt Only. If Non EFG / SFLG Lender Debt Fully Repaid And Surplus Security Funds Exists From This Source, Repay To The Borrower / Personal Guarantor
Do Any Of The Security Realisation Monies Relate To Linked Collateral Taken At The Same Time As The EFG Loan Was Granted ?
No
Yes
75% Of These Security Proceeds To Be Reimbursed To CfEL.Remaining 25% Stays With Lender.
All Remaining Security Proceeds To Be Used To Repay Non EFG Debt Of Lender First. Once This Debt Is Fully Repaid, Any Remaining Security Proceeds To Be Split 75% / 25% To CfEL / Lender Respectively.

7.5 Key Differences in Demands and Recoveries Rules for EFG and SFLG

In the circumstances leading to the need to **make a Guarantee Claim**, Lenders must follow their **normal commercial practice**, subject to noting the following scheme-specific parameters:

Criterion or Defining Characteristic	**Legacy SFLG**	**New SFLG**	**EFG**
Defining Loan Offer Period for respective schemes	Up to 30th November 2005 (NB loans Offered prior to 1st April 2003 subject to different Guarantee Rates)	Loans offered on or after 1st December 2005	Loans and other facilities offered from 14th January 2009
Entitlement to add fees and / or charges to the outstanding loan balance for the purposes of the claim	None	None	None
Entitlement to claim interest	Up to 9 months of accrued interest counted back from date of Guarantee Claim or date when Borrower ceased to meet interest payments, whichever is the shorter	Up to 6 months of accrued interest counted back from date of Guarantee Claim or date when Borrower ceased to meet interest payments, whichever is the shorter	None, except in respect of Overdraft and invoice Finance Guarantee Facilities (Types E and F), for which interest accrued prior to the earlier of Demand on the Borrower and the Facility Expiry Date may be included in the Guarantee Claim
Entitlement to claim fixed rate break costs (where specified in the Facility Letter)	Up to 1.25% of the outstanding capital balance per remaining year of the fixed interest rate	None	None

Criterion or Defining Characteristic	**Legacy SFLG**	**New SFLG**	**EFG**
Timeframe within which Claim must be made	Within 12 months of Demand on Borrower	Within 6 months of Demand on Borrower	Within 24 months of Demand on Borrower. Claims may be made sooner where the recovery process has been completed, or after 18 months, if the process remains incomplete
Basis of Guarantee Claim Calculation *(NB: The Web Portal performs calculation based on component variables input by Lender. Do not attempt to "mix" calculation on and off Web Portal)*	Outstanding Capital at Default *Plus* Up to 9 months accrued interest *Plus* Any eligible break costs *All multiplied by* The Guarantee Percentage (75% from 1st April 2003, either 70% or 85% previously. Web Portal holds Guarantee Percentage information)	Outstanding Capital at Default *Plus* Up to 6 months accrued interest *All multiplied by* The Guarantee Percentage (always 75%)	Outstanding Capital at Default *Plus* Eligible Interest (Types E and F only) *All multiplied by* The Guarantee Percentage (always 75%)
Web Portal Entry (NB: This guidance intended specifically for staff familiar with the use of the Web Portal)	Enter component variables of calculation separately as instructed. Web Portal automatically applies the applicable Guarantee Percentage and calculates Claim value	Enter component variables of calculation separately as instructed. Web Portal automatically applies the 75% Guarantee Percentage and calculates Claim value	Enter component variables of calculation (net of any security realisations, etc) as instructed. Web Portal automatically applies the 75% Guarantee Percentage and calculates Claim value

When **realising security and undertaking other recovery action**, Lenders must follow their **normal commercial practice**, subject to noting the scheme-specific parameters:

Criterion or Defining Characteristic	**Legacy SFLG**	**New SFLG**	**EFG**
Is it permissible to make a Claim while Security Realisation and Recovery actions are still underway?	Yes	Yes	Yes, but only once at least 18 months have elapsed from the date of Demand on Borrower. (NB: If all Recovery actions have been completed in under 18 months then Claim may be made immediately)
Is it permissible to deduct Security Realisation and Recovery costs from proceeds prior to entering the scheme Claim and / or Post-Settlement Recoveries process?	Yes – All reasonable costs may be deducted from the proceeds received	Yes – All reasonable costs may be deducted from the proceeds received	Yes – All reasonable costs may be deducted from the proceeds received
Are there any assets / recoveries, whether Charged or Uncharged, which are specifically excluded from consideration?	Any security where the charge form does not have an "all monies and liabilities" clause Any personal asset not used in the business (although if the Lender assumes 'see through' to the background assets of a sole trader when making an initial credit decision, all background personal assets are assumed to be used as part of the business)	Any security where the charge form does not have an "all monies and liabilities" clause Any personal asset not used in the business (although if the Lender assumes 'see through' to the background assets of a sole trader when making an initial credit decision, all background personal assets are assumed to be used as part of the business)	Principal Private Residence

Is the Lender permitted to deduct from proceeds any interest on an outstanding commercial debt which has accrued since the date of Claim on Guarantee before apportioning Post-Settlement Recovery proceeds?	Yes	Yes	No
Priority for Security Realisation and Recovery proceeds received *(NB: Web Portal performs calculation based on component variables input by Lender. Do not attempt to "mix" calculation on and off Web Portal)*	Lender Commercial Debt issued prior to or simultaneous with SFLG Debt ranks ahead of SFLG Lender Commercial Debt issued after SFLG Debt ranks on an equal basis with SFLG Debt However, prior to signature of the agreement migrating management of Legacy SFLG cases to the Web Portal, Lenders had and in the majority of cases exercised the right to request on a case by case basis that the ranking of subsequent Lender Commercial Debt be altered so that it ranked ahead of SFLG Debt	Lender Commercial Debt issued prior to or simultaneous with SFLG Debt ranks ahead of SFLG Lender Commercial Debt issued after SFLG Debt ranks on an equal basis with SFLG Debt Remaining recoveries are then apportioned pro-rata between the outstanding balances of the subsequent Commercial and SFLG Debts The proportion of the recovery to be refunded to BIS is therefore determined by the formula: **(A/(A+B)) x C x 75%**	Note the importance of TWO distinctions: a) Timing – whether recoveries were made prior or subsequent to a Guarantee Claim having been made; and, b) Type – for each timing case, whether the recoveries arise from Linked Collateral or from other proceeds **<u>RECOVERIES MADE PRIOR TO GUARANTEE CLAIM</u>** **1 – From Linked Collateral** Apply proceeds from Linked Collateral to EFG Debt except if there is also Commercial Debt issued simultaneously, in which case apply proceeds to linked Commercial Debt first with any

	Remaining recoveries are then apportioned as for New SFLG (next column), except that in practice where the concession regarding the ranking of subsequent Commercial Debt has been invoked then B = 0 and thus those recoveries are attributable in full to the SFLG Debt. The proportion of the recovery to be refunded to BIS is dependent upon the Guarantee Percentage applicable to the loan concerned. (This is 75% in most remaining cases, but 70% or 85% in respect of loans Offered before 1st April 2003)	Where: A = outstanding SFLG exposure at Date of Guarantee Claim B = outstanding subsequent Lender Commercial Debt at time of recovery C = total recovered funds available	surplus funds thereafter applied to EFG Debt **2 – All other proceeds** Lender Commercial Debt issued prior to or simultaneous with EFG Debt ranks ahead of EFG for receipt of recovery proceeds Lender Commercial Debt issued after EFG Debt ranks on an equal basis Recoveries are apportioned pro-rata between the outstanding balances of the subsequent Commercial and EFG Debts. The proportion of the recovered funds attributable to reducing the outstanding EFG exposure is therefore determined by the formula: **(A/(A+B)) x C** Where: A = outstanding EFG exposure at time recoveries are received B = outstanding subsequent Lender Commercial Debt

			C = total recovered funds available After this apportionment has been made a Guarantee Claim should then be made for 75% of the remaining EFG exposure. **<u>RECOVERIES MADE AFTER GUARANTEE CLAIM</u>** **1 – From Linked Collateral** Apply proceeds from Linked Collateral to EFG Debt except if there is also Commercial Debt issued simultaneously, in which case apply proceeds to linked Commercial Debt first with any surplus funds thereafter applied to EFG Debt. 75% of proceeds attributable to EFG Debt are to be refunded to BIS. **2 – All other security realisation and recovery proceeds** Lender Commercial Debt issued prior to or simultaneous with EFG Debt ranks ahead of EFG for receipt of recovery proceeds. Lender Commercial Debt issued

			after EFG Debt ranks on an equal basis. Recoveries are apportioned pro-rata between the outstanding balances of the subsequent Commercial and EFG Debts. The proportion of the recovery to be refunded to BIS is therefore determined by the formula: **(A/(A+B)) x C x 75%** Where: A = outstanding EFG exposure on which the Guarantee Claim was based B = outstanding Lender Commercial Debt at time recovery was made C = recovery funds available After this calculation has been performed the refund due to BIS should be paid through the established quarterly Demand Invoice and Recoveries Statement process

Web Portal entry *The Web Portal will calculate any refund due to BIS based upon data input by Lender* *(NB: This guidance intended specifically for staff familiar with the use of the Web Portal)*	Enter component variables (i.e. B and C above, also interest and break costs) of calculation separately as instructed. Web Portal automatically applies the applicable Guarantee Percentage and calculates refund value	Enter component variables (i.e. B and C above, also interest) of calculation separately as instructed. Web Portal automatically applies the applicable Guarantee Percentage and calculates refund value	Enter component variables of calculation separately as instructed. • Outstanding non-EFG Debt; • Post-settlement realisations excluding Linked Collateral; and, • Linked Collateral. Portal automatically applies the applicable Guarantee Percentage and calculates refund value

7.6 The Claim Limit

The Lender can claim up to 75% of the outstanding principal amount of any individual EFG facility, subject to a "cap" on total claims arising from a Lender's portfolio.

The "portfolio" in this instance refers to all loans Offered within the specific EFG Phase, running from 1 April to 31 March the following year. This overall cap arose from a need to comply with European State Aid rules.

Definitions and Explanations

- Annual Drawn Lending: The total value of lending undertaken within a EFG Phase in connection with which the Lender may call upon the EFG.

- Guaranteed Percentage: The proportion of the principal amount of any guaranteed EFG facility which is protected by the EFG. Currently 75%.

- Gross Default Limit: The maximum default rate covered by EFG against any annual portfolio of drawn lending. Currently 20%.

- Annual Claim Limit: The total value of claims to BIS which may be made arising from defaults of EFG facilities made within the corresponding Annual Drawn Lending. The Annual Claim Limit is, therefore, linked to the year of lending and not to the year in which the claim arises.

7.6.1 Claim Limit for Loans Offered up to 31 March 2011

- The Claim Limit for Phase 1 (from 14 January 2009 to 31 March 2010) and Phase 2 (from 1 April 2010 to 31 March 2011) was 9.75% (equivalent to a maximum default rate of 13%. This can be explained:

Guaranteed Percentage (75%) x Annual Drawn Lending x Gross Default Limit (13%)

or

9.75% of the Annual Drawn Lending

The Effective Guarantee Rate of EFG after Applying the Annual Claim Limit

The following table demonstrates the effective guarantee rate of the EFG when the value of claims is restricted as a result of the Claim Limit.

Where a Lender's EFG portfolio has a net bad debt rate (after recoveries) of 13% or less, the EFG will cover 75% of the loss. Thereafter the effective rate falls, to 48.75% where the net bad debt rate is 20%, to a minimum of 9.75% should there be a 100% net bad debt rate. The table uses as an example portfolio of EFG lending of £1m.

EFG Guarantee Rate	75%					
Portfolio Claim Limit	9.75%					
EFG Portfolio Lending	1,000,000					
Value of 9.75%	97,500					
Bad Debt Rate on EFG Portfolio (net of recoveries)	5.0%	10.0%	13.0%	20.0%	50.0%	100%
Value of Net Bad Debts	50,000	100,000	130,000	200,000	500,000	1,000,000
Max Value of EFG Claims at 75%	37,500	75,000	97,500	150,000	375,000	750,000
Max Claimable Amount (capped at £97.5k)	37,500	75,000	97,500	97,500	97,500	97,500
Effective EFG Guarantee Rate	**75.0%**	**75.0%**	**75.0%**	**48.75%**	**19.5%**	**9.75%**

Worked Example

- For the year to 31 March 2011, the Anytown Bank was allocated an Annual Lending Limit (see section 8.1) of £20m giving a corresponding Annual Claim Limit of £1.95m (£20m x 9.75%).
- By the end of the period, the Anytown Bank has made eligible loans of £18m. The Claim Limit is, therefore, capped at £1.755m (£18m x 9.75%).

- The Anytown Bank subsequently experiences defaults arising from those loans and makes claims as itemised in the table below:

Year to 31 March	Defaults net of recoveries (£k)	75% of exposure (£k)	Amount claimed (£k)	Balance of Claim Limit (£k)
2011	0	0	0	1755
2012	1200	900	900	855
2013	600	450	450	405
2014	400	300	300	105
2015	300	225	(*)105	0
2016	100	75	(")0	0

(*) Although 75% of the Anytown Bank's exposure in 2015 is £225k there is only £105k of the Annual Claim Limit remaining and so the amount which may be claimed is capped at £105k, with Anytown Bank bearing the remaining £120k loss.

(") Although 75% of the 2016 exposure is £75k there is no Annual Claim Limit remaining and so the Anytown Bank must bear the full exposure.

In total, of £2.6m of net bad debts, the Lender was able to claim £1.755m under the guarantee, translating into an effective guarantee rate of 67.5%.

7.6.2 Claim Limit from 1 April 2011 to 31 March 2012

A two-tier Claim Limit is applicable to all new lending from 1 April 2011 to 31 March 2012 (Period 3). A higher claim limit (20% gross default/15% net claim) was introduced for the first £1m of each Lender's lending with a lower limit (12.3% gross default/9.225% net claim) applying subsequently, maintaining the existing 13% gross / 9.75% net at the level of the programme overall.

The following table shows the effective guarantee rates for a Lender with £1m of lending in an allocation period, where the Claim Limit is 15%.

EFG Guarantee Rate	75%					
Portfolio Claim Limit (up to £1m of lending)	15.00%					
EFG Portfolio Lending	1,000,000					
Value of 15%	150,000					
Bad Debt Rate on EFG Portfolio (net of recoveries)	5%	10%	15%	20%	50%	100%
Value of Net Bad Debts	50,000	100,000	150,000	200,000	500,000	1,000,000
Max Value of EFG Claims at 75%	37,500	75,000	112,500	150,000	375,000	750,000
Max Claimable Amount (capped at £150k)	37,500	75,000	112,500	150,000	150,000	150,000
Effective EFG Guarantee Rate	**75.00%**	**75.00%**	**75.00%**	**75.00%**	**30.00%**	**15.00%**

The following table shows the effective guarantee rates for a Lender with £10m of lending in an allocation period. For a £10m Lender the Claim Limit has increased marginally to 9.80%. As shown, an effective Claim Limit of almost 50% will operate at a 20% default level.

EFG Guarantee Rate	75%					
Portfolio Claim Limit on first £1m of lending	15.000%					
Portfolio Claim Limit after £1 million	9.225%					
EFG Portfolio Lending	10,000,000					
Portfolio Claim Limit on first £1m of lending	150,000					
Portfolio Claim Limit for remaining £9m	830,250					
Aggregate Claim Limit	**980,250**					
Effective Overall Claim Limit	9.80%					
Bad Debt Rate on EFG Portfolio (net of recoveries)	5.00%	10.00%	13.00%	20.00%	50.00%	100%
Value of Net Bad Debts	500,000	1,000,000	1,300,000	2,000,000	5,000,000	10,000,000
Max Value of EFG Claims at 75%	375,000	750,000	975,000	1,500,000	3,750,000	7,500,000
Max Claimable Amount (capped at £97.5k)	375,000	750,000	975,000	980,250	980,250	980,250
Effective EFG Guarantee Rate	**75.00%**	**75.00%**	**75.00%**	**49.01%**	**19.61%**	**9.80%**

7.6.3 Claim Limit from 1 April 2012 to 31 March 2014

In the Budget on 21 March 2012, Government announced a temporary change to the Claim Limit for all new lending from 1 April 2012 to 31 March 2013 (Phase 4), with the higher claim limit (20% gross default/ 15% net claim) extended to apply to all lending, not just the first £1m.

Although originally intended as a temporary measure, this Claim Limit structure was continued for all Phase 5 lending (from 1 April 2013 to 31 March 2014).

The following table again shows the effective guarantee rates for a Lender with £1m of lending in an allocation period, where the Claim Limit is 15%.

EFG Guarantee Rate	75%					
Portfolio Claim Limit (up to £1m of lending)	15.00%					
EFG Portfolio Lending	1,000,000					
Value of 15%	150,000					
Bad Debt Rate on EFG Portfolio (net of recoveries)	5%	10%	15%	20%	50%	100%
Value of Net Bad Debts	50,000	100,000	150,000	200,000	500,000	1,000,000
Max Value of EFG Claims at 75%	37,500	75,000	112,500	150,000	375,000	750,000
Max Claimable Amount (capped at £150k)	37,500	75,000	112,500	150,000	150,000	150,000
Effective EFG Guarantee Rate	**75.00%**	**75.00%**	**75.00%**	**75.00%**	**30.00%**	**15.00%**

7.6.4 Claim Limit from 1 April 2014 to 31 March 2015

A two-tier Claim Limit will be applicable to all Phase 6 lending (from 1 April 2014 to 31 March 2015).

To assist smaller lenders, a higher claim limit (100% gross default/75% net claim) will apply for the first £100k of each Lender's lending with a lower limit (20% gross default/15% net claim) applying subsequently.

In addition, **for Type F and Type H (invoice finance) facilities only,** the Annual Drawn Lending value will be calculated as the annual Type F and Type H additional EFG limits multiplied by the prevailing IAUR.

EFG Guarantee Rate	75%					
IAUR	60%					
Portfolio Claim Limit on first £100k lending	75%					
Portfolio Claim Limit after £100k	15%					
EFG Portfolio Lending	10,000,000					
Of which Type F and Type H represent	1,000,000					
Annual Drawn Lending 'equivalent'	**9,600,000 ***					
Portfolio Claim Limit on first £100k of lending	75,000					
Portfolio Claim Limit for remaining £9.5m	1,425,000					
Aggregate Claim Limit	**1,500,000**					
Effective Overall Claim Limit	15.625%					
Gross Default Rate on EFG Portfolio (net of recoveries)	5.00%	10.00%	13.00%	20.00%	50.00%	100%
Value of Net Bad Debts	500,000	1,000,000	1,300,000	2,000,000	5,000,000	10,000,000
Max Value of EFG Claims at 75%	375,000	750,000	975,000	1,500,000	3,750,000	7,500,000
Max Claimable Amount	375,000	750,000	975,000	1,500,000	1,500,000	1,500,000
Effective EFG Guarantee Rate	**75.00%**	**75.00%**	**75.00%**	**75.00%**	**30.00%**	**15.00%**

* Calculated:
10,000,000 – 1,000,000 = 9,000,000
plus: 1,000,000 x 60% = 600,000
Annual Drawn Lending 'equivalent' = 9,600,000

Claim Limit Management for Small Lenders

- A 'Small Lender' is defined as a Lender which, for an Annual Scheme Period, has:
  a) an Annual Base Lending Allocation of no more than £2 million; and
  b) indicated that it expects to make less than 50 Scheme facilities available during the EFG Phase.

- It is recognised that the Claim Limit can present concentration problems for funders with small portfolios. To improve the working of the Claim Limit for Small Lenders, for lending guaranteed in Phases 6 and onwards unutilised Small Lender Claim Limits will 'carry forward' to subsequent Phases.

- 'Carry forward' of unused Claim Limit will provide these Small Lenders with certainty that, where they have surplus Claim Limit in any Phase (i.e. all of the Lender's facilities for that Phase are either repaid or have failed leading to a claim under the Guarantee), they may roll forward that surplus Claim Limit and add it to the available Claim Limit for the subsequent Phase. This rolling forward continues for as long as there is a surplus Claim Limit.

8 General Information for Lenders

8.1 Annual Lending Limits

Each Lender is allocated an "Annual Lending Limit", which is the maximum level of drawn facilities the Lender can make by the time the scheme fully closes.

Increasing the Annual Lending Limit

In the event that a Lender exceeds its Annual Lending Limit, any further facilities processed via the Web Portal are not automatically covered by the EFG. There is, however, some flexibility in the scheme. The Lender may be able to lend more money than originally agreed for a specific period by applying for an increase in allocation as follows:

- The Lender formally asks BBB for permission to provide more EFG facilities by making a Specific Lending Limit Proposal, saying exactly how much more the Lender would like to lend. The application must be submitted in hard copy, addressed to Judith Ozcan, MD Debt of BBB;

- The Specific Lending Limit Proposal should set out in detail why the Lender wants to provide more facilities and include a brief business plan explaining the specific purposes for which the extra lending will be utilised; and,

- The Lender can provide more lending for a number of reasons, including:
    - enabling the Lender to help more businesses;
    - targeting particular types of business;
    - targeting particular regions in the UK; or,
    - targeting high growth businesses.

BBB may ask the Lender for more information. BBB will then write to the Lender to say whether or not the Lender can provide more lending under the scheme, and under what conditions. This ability to provide more lending under EFG is known as the Specific Lending Limit.

8.2 Transferring Rights and Change of Ownership

Transferring Rights under the EFG Legal Agreement to another Party

Any proposed transfer can only occur with the prior written consent of the Secretary of State. Lenders should contact BBB at the earliest opportunity if this situation were to arise.

Transferring Rights under the EFG Legal Agreement to another Group Company

Any proposed transfer can only occur with the prior written consent of BBB. Lenders should contact BBB at the earliest opportunity if this situation were to arise.

Change of Ownership within the Lender Organisation

A change in shareholding in a Lender does not change its legal personality and, therefore, there is no impact on the EFG Legal Agreement.

8.3 Leaving the EFG Programme

Either the Lender or BIS can give 6 months written notice to end the EFG Legal Agreement and neither party needs to provide any reason for doing so. Once the EFG Legal Agreement has come to an end, the Lender is no longer entitled to provide new EFG facilities. Existing guarantees and the ability to claim under the guarantee scheme for existing EFG facilities provided up to the date of termination would remain in place.

8.4 The Lender Audit Programme

8.4.1 Introduction

Audits are a key feature of the EFG scheme and the Government can carry out an audit of the Lender's activities in relation to the scheme at any time. This is to ensure the Lender is running the scheme properly. The audit must be carried out during the Lender's usual working hours and BBB must give at least five working days' notice.

The Lender shall provide all reasonable assistance to BBB (or its External Auditor) in carrying out the audit, including provision of all relevant documentation in relation to individual facilities and the investigation of enquiries raised by BBB (or its External Auditor) during the audit process.

A senior representative of the Lender must be available to discuss the audit findings prior to the publication of the Audit Report. The Lender and its employees must do all they can to cooperate with the people carrying out the audit. This includes providing information and documents as requested.

A high volume Lender (under the EFG scheme) can be expected to be subject to an audit twice a year, a lower volume Lender no more than once a year.

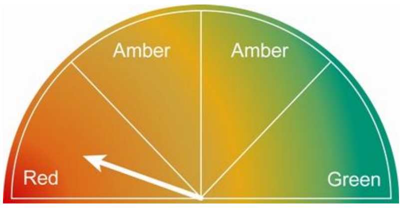
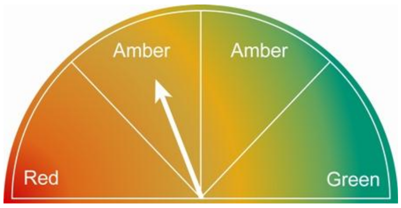
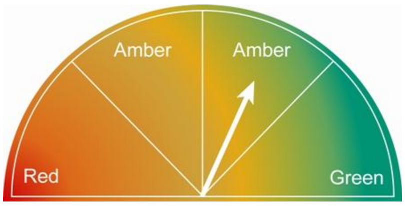
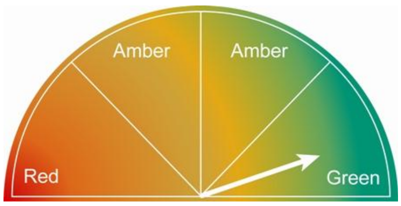
8.4.2 Audit Objectives and Risks to be Identified

Audits focus on the following objectives and risks:

Objectives	Risks
EFG Eligibility: Completeness, Accuracy and Integrity of Portal Data and Compliance with the Legal Agreement:	Loans are provided to businesses that are ineligible for the EFG scheme. The Offer has not been made in accordance with the Legal Agreement or the Web Portal data is inaccurate.
EFG and SFLG Demands and Recoveries: Completeness, Accuracy and Integrity of Portal Data and Compliance with the Legal Agreement:	Defaults are not identified and acted upon in a timely manner. Data on the Web Portal regarding Demands is inaccurate. Demands made on the Secretary of State are inaccurate or invalid under the terms of the Legal Agreement.
Application of the Lender's Normal Commercial Lending Process:	The Lender has not complied with their usual commercial lending process when processing EFG applications, in terms of viability assessment and security availability assessment, on-going monitoring and control.
Lender's Control and Governance, including Training and Dissemination of Information and Guidance to Staff:	Lack of control over EFG and SFLG processes leading to non-compliance with the Legal Agreement, and inconsistent approaches taken by staff. Staff are not aware of their responsibilities or how to carry out their duties effectively. Poor segregation of duties and lack of control over Web Portal access rights leads to inaccurate input of data. Poor decision making results from poor quality information available to management.

8.4.3 Audit Grades

Each Lender receives an overall assurance level, as well as a separate grade for each of the (up to) four key objective areas. New terminology to grade the assurance levels in audit reports were introduced in 2011:

<table>
<tr><th>Overall Opinion</th><th>Definition</th></tr>
<tr><td>
</td><td>Red
Taking account of the issues identified, BBB cannot take assurance that the controls upon which the Lender relies to manage the EFG and SFLG scheme are suitably designed, consistently applied or effective. Action needs to be taken to ensure that risks are managed.</td></tr>
<tr><td>
</td><td>Amber / Red
Taking account of the issues identified, whilst BBB can take some assurance that the controls upon which the Lender relies to manage the EFG and SFLG scheme are suitably designed, consistently applied and effective, action needs to be taken to ensure that risks are managed.</td></tr>
<tr><td>
</td><td>Amber / Green
Taking account of the issues identified, BBB can take reasonable assurance that the controls upon which the Lender relies to manage the EFG and SFLG scheme are suitably designed, consistently applied and effective. However, issues have been identified that, if not addressed, increase the likelihood of risks materialising.</td></tr>
<tr><td>
</td><td>Green
Taking account of the issues identified, BBB can take reasonable assurance that the controls upon which the Lender relies to manage the EFG and SFLG scheme are suitably designed, consistently applied and effective.</td></tr>
</table>

Recommendations in the audit reports are now categorised as follows:

High – action is imperative to ensure that the objectives for the area under review are met.
Medium – requires action to avoid exposure to significant risks in achieving the objectives for the area under review.
Low – action advised to enhance control or improve operational efficiency.

A fourth category of recommendation has also now been introduced. The **Suggestion** categorisation allows the External Auditor to include any value for money enhancements identified during the course of testing and any Lender feedback received regarding the EFG and SFLG scheme operation as a whole.

8.4.4 Evidence Required to Provide Green Assurance

A "Green" assurance grade is only possible if the Lender can demonstrate to the External Auditor that the objectives are being met. Lenders are, therefore, encouraged to be especially careful to ensure that loan files are complete with all appropriate supporting evidence.

Eligibility

- The Lender needs to be able to provide evidence that according to normal commercial lending criteria the proposition is viable, but that absence or inadequacy of security makes the proposal unsupportable.
- Where any decisions are borderline, additional evidence should be provided to give a persuasive and robust argument that the loan is valid for EFG and that all eligibility criteria (for EFG) have been satisfied. An example may be where the Lender is proposing an EFG to a loss making enterprise.
- We would also expect evidence to be available to reflect the choice of EFG type, especially where Type D EFG is concerned.

Monitoring

- The External Auditor is likely to seek evidence that monitoring of an EFG is being undertaken in-line with the loan agreement.
- All Conditions Precedent were satisfied prior to drawdown, all security was correctly perfected and that on-going monitoring was as specified.

Demands and Recoveries

- The Lender should seek to provide full details of the circumstances of a Claim and clear evidence as to the calculation of a Claim. Where relevant, evidence should be provided detailing attempts to make Recoveries.

Documentation

- It is imperative that documentation proving eligibility and Demands is available at audit.
- Where cases are borderline the Lender should make efforts to provide additional documentation to justify the use of EFG. In some circumstances, additional documentation will need to be provided when Demand on the Borrower occurs shortly following drawdown (see Enhanced Audit, below).
- Where Type D EFG is used, it is requested that Lenders ensure that file notes provide detailed notes explaining the rationale behind the use of EFG.
- Lenders are encouraged not simply to respond to the External Auditor's documentary requests, but to pro-actively volunteer any documentation that may be relevant to the case.

8.5 Enhanced Audit

8.5.1 Introduction

The general audit described above examines both general lender practices and a sample of facilities for both eligibility, and Demands and Recoveries. The Enhanced Audit looks closely at EFG cases where the time between draw down and Lender Demand is less than six months. The purpose of this Enhanced Audit is to ensure that any Guarantee Claim to BIS is fully justified; therefore, the External Auditor examines all stages of the loan process from eligibility checking to Demands and Recoveries, and any subsequent Guarantee Claim.

The Enhanced Audit is led by the External Auditor, with some cases also reviewed by BBB.

8.5.2 Documentation to be Provided by the Lender

Shortly following the quarter end, the External Auditor will advise the Lender of any EFG cases which have been selected for Enhanced Audit. The Lender will be asked to provide a pack of information on the Borrower, addressing the following areas:

Viability	Explain why the proposition was deemed viable, according to normal commercial lending criteria at the time of draw down. Comment on how actual results post draw down differed from forecast results.
Security	Summarise the security available at the time of draw down and, where appropriate, provide commentary with regards to the inadequacy of such security (with regards to normal commercial lending criteria). Make reference to any specific documentation / correspondence as appropriate.
Eligibility	Summarise how the proposition met EFG criteria in terms of business size, facility purpose and business location.
Terms of Sanction and Conditions Precedent	What were the Terms of Sanction and Conditions Precedent and were these satisfied? Provide further commentary where appropriate (especially if a Conditions Precedent was not met). Make references to documentation where appropriate.

The Lender will be requested to provide the following supporting documentation:

- EFG Credit Application (and any subsequent papers)
- Terms of Sanction and Conditions Precedent
- Statutory accounts
- Management accounts up to and post draw down
- Forecasts

- Summary of security
- Facility Letter
- IBR report (if issued within 6 months of EFG sanction), plus evidence that any points raised have been addressed by the Lender
- A copy of the Lender's own internal report on the reason for business failure
- Liquidator / Administration Report
- The Lender's diary system notes
- Any other information the Lender considers necessary to support the points made in the lending summary above

To assist document sharing between the staff at the Lender, the External Auditor and BBB, **all supporting documentation must be provided in electronic format** such as a pdf file. Each document should be provided in a separate named file.

The Enhanced Audit is likely to be delayed until the relevant documentation has been provided, which may impact upon the timing of any settlement of any Claims on the Guarantee.

8.5.3 The Enhanced Audit Appraisal

The Enhanced Audit specifically examines the eligibility of the facility to benefit from EFG backing at the time of draw down. The Enhanced Audit, therefore, focuses on the technical eligibility and also whether the Lender has applied its normal commercial lending practice in making the lending decision, and in allowing draw down at the specific point in time.

Recent examples of facilities which have not passed these criteria include facilities where:

- **Recoveries** – The Lender failed to provide sufficient evidence that its normal recoveries procedures were followed or adhered to EFG rules in respect of the priority for distribution of recovery proceeds;
- **Security** – The Lender failed to provide sufficient evidence that prior to the provision of the EFG facility the availability of business or personal assets were fully investigated or normal policies or EFG rules relating to the charging or discounting of any available assets were followed;
- **Viability** – The Lender failed to provide sufficient evidence that its normal policies regarding viability were followed;
- **Conditions Precedent** – The Lender failed to provide sufficient evidence that all Conditions Precedent were satisfied prior to draw down; and,
- **Ineligible Borrower** – The Lender used EFG in support of an ineligible Borrower (i.e. the core of the Borrower's activity was located overseas).

8.5.4 First and Second Reviews

BBB will notify Lenders in writing where Claims on the Guarantee have been approved or otherwise. Where the appraisal concludes that there is insufficient evidence to prove eligibility, reasons will be provided and the Lender will be given the opportunity to address the issues raised in a second review.

It is intended that first and second reviews will be completed within the quarter following the quarter in which the Claim is made on the Guarantee. Any Claims that are approved are to be re-submitted on the next Demand Invoice. Note that where payment is declined, any such amount is not deducted from the Lender’s Claim Limit (i.e. another subsequent Claim can “take the place” of any Claim which is deemed ineligible.)

8.6 Annual Reports

If a Lender provides more than 100 facilities during each EFG period, it may be required to provide BBB with an Annual Report providing information on how the Lender has operated the scheme.

8.7 Non-Compliance with EFG Scheme Rules

If BBB believes that a Lender is breaking one or more of the rules of the scheme, a meeting may be set up to agree what can be done to remedy the situation.

If the Lender continues to break the rule or is in serious breach of the rules, BBB may tell the Lender what it must do to be able to remain in the scheme. The ultimate sanction would be termination of the Lender's participation in the scheme. BBB can do this with immediate notice in writing.

8.8 External Service Level Agreement

BIS will enter into agreements, known as Service Level Agreements, with other organisations in order to properly implement and operate the scheme – for example: the host of the EFG Web Portal, in relation to confidentiality and its availability, reliability and maintenance; the independent Premium Collection Agent, in relation to the collection of the Scheme Guarantee Premium; the External Auditor, in relation to the general and Enhanced Audits.

8.9 Data Protection Act

BIS and the Lender agree that they will follow the requirements of the Data Protection Act 1998.

The Lender and BIS must take every step to ensure that only necessary information about Applicants and their businesses is kept and recorded, and that this information is held on a secure system.

Both the Lender and BIS have agreed appropriate remedies in the event of any incident occurring where loss has been suffered because personal information has been lost or misused in contravention of the Data Protection Act.

8.10 EFG Web Portal Rights

BIS own the intellectual property associated with the Web Portal functionality. BIS uses the information within the Web Portal to manage the programme effectively.

8.11 Marketing and Promotion

If the Lender decides to market the EFG scheme on the Lender's own website, the Lender undertakes to ensure that all details regarding EFG are at all times as up-to-date and accurate as possible.

The Lender shall ensure that any marketing material utilised in respect of the EFG scheme includes a clear provision to the effect that, in making the scheme available, there is no implication of endorsement or warranty of the Lender by the Government.

9 Appendices

9.1 Sample Data Protection and Disclosure Declaration Letter

"I give my permission to the Lender and the Government to:

- make any enquiries about my EFG application
- take up references about me and my business
- give information to each other about me and my business
- give information to any official involved in running or monitoring the EFG."

Signature Section

Signed	Signed
Print Name	Print name
Position	Position
Date	Date

Signed in accordance with the requirements of the Lender's normal commercial lending practice. Otherwise, for a limited company two signatories are required, being two Directors or one Director and the Company Secretary. For a partnership, all partners must sign.

9.2 Sample State Aid Letter

EFG STATE AID LETTER TO BE SENT TO BORROWER ON LENDER'S LETTERHEAD AS PART OF THE FACILITY DOCUMENTATION

Applicant Name

Applicant Address

Date

ENTERPRISE FINANCE GUARANTEE – NOTIFICATION OF STATE AID

Applicant:	***XXXX Ltd***
Lender:	***Little Tinkers***
EFG Facility Reference Number:	***W5A39KG+01***
Facility amount (£):	***123,456.00***
Guarantee Term (months):	***120***

Dear Sirs,

Our ability to provide you with this facility has been dependent upon a guarantee we have received from the Department for Business, Innovation & Skills (BIS) under the Enterprise Finance Guarantee (EFG) scheme. The assistance provided through EFG, like many Government-backed business support activities, is regarded as a State aid and is deemed to benefit you as it has enabled us to provide you with a facility which would not otherwise have been possible.

Provision of such State aid is governed by regulations made by the European Commission, details of which may be found in the Annex at the end of this letter. Under these rules the maximum State aid any undertaking may receive over any rolling three-year period is generally €200,000, although lower ceilings apply in certain sectors as detailed in the Annex.

The value of the *de minimis* aid arising from this facility is €***14,773.57***

It is your responsibility to retain records of any State aid arising from assistance received for a minimum of ten years from the date of receipt and to ensure that you do not exceed the rolling three-year limit. If you make any other application to a support scheme which is deemed to provide State aid during the next three years you will be required to inform the operator of that scheme about the State aid advised by this letter and any other applicable aid from other sources.

Please note that this letter is issued solely to advise you of the value of the State aid arising from your facility and does not in any way alter any of the terms of our facility letter to you, nor is it a notice of further funding.

Yours sincerely,

ANNEX – DETAIL OF RELEVANT EUROPEAN COMMISSION REGULATIONS

This information is provided for clarification and guidance.

Sector	Maximum Permissible Aid (€)	Relevant Regulation	Regulation Date
Agriculture	15,000	1408/2013	18/12/13
Fisheries and Aquaculture	30,000	875/2007	24/7/07
Road Transport	100,000	1407/2013	18/12/13
All Other Eligible Sectors	200,000	1407/2013	18/12/13

The “rolling three-year limit” is defined as follows:

a) when considering the impact of previous aid on the provision of the present facility, the current fiscal year and the two preceding fiscal years; or
b) when considering the impact of the aid attributable to the present facility on any future applications for aid, the current fiscal year and the two subsequent fiscal years.

With the “current fiscal year” being the fiscal year in which the date of the facility letter for the present facility falls, with each EFG fiscal year running from 1st April to the following 31st March.

An “undertaking” is defined as any entity engaged in economic activity, regardless of its legal status and the way in which it is financed. All entities controlled (on a legal or *de facto* basis) by the same entity are considered to be a single undertaking and thus collectively subject to the same single maximum permissible aid ceiling.

9.3 Sample Premium Payment Schedule

Premium Schedule for W5A39KG+01

State: Complete

Amount: £123,456.00

Last Modified: 26/05/2009 11:15

Business Name: XXXX Ltd

User: Administrator

Lender: Little Tinkers

This Schedule itemises the cost of the Premiums that you (the Borrower) will be paying to the Government each quarter for the duration of this loan. The first direct debit payment is due shortly after the loan is drawn down. Future payments are collected quarterly, with collection being made on or around the 14th of the month.

Amount of Initial Premium Payment: £617.28

You must include a completed Direct Debit Mandate when you accept the loan you have been offered.

Month of Second Direct Debit Premium Collection:

Subsequent Direct Debit Premiums to be Collected: £12,962.88

Total Premium Payable over the Life of the Loan: £13,580.16

Premium No.	Premium Amount	Premium No.	Premium Amount
1	£333.66	21	£332.54
2	£617.28	22	£316.98
3	£617.28	23	£300.30
4	£617.28	24	£283.62
5	£600.60	25	£266.93
6	£583.91	26	£250.25
7	£567.23	27	£233.57
8	£550.55	28	£216.88
9	£533.86	29	£200.20
10	£517.18	30	£183.52
11	£500.50	31	£166.83
12	£483.81	32	£150.15
13	£467.13	33	£133.47
14	£450.45	34	£116.78
15	£433.76	35	£100.10

16	£417.08	36	£83.42
17	£400.40	37	£66.73
18	£383.71	38	£50.05
19	£367.03	39	£33.37
20	£350.35	40	£16.68

Schedule based on the following information:

What is the expected year of the initial draw? (yyyy)

What is the date of the Premium Collection point from which this schedule applies? (dd/mm/yyyy)

What is the amount of the initial draw? £ 123,456.00

What is the loan term in months remaining at this Premium Collection point? 120

What is the length of the initial capital repayment holiday? (Months): 9

What is the amount of the additional draw? (Second tranche): £

What is the number of months (from this Premium Collection point) to second tranche drawdown?

What is the amount of the additional draw? (Third tranche) £

What is the number of months (from this Premium Collection point) to third tranche drawdown?

What is the amount of the additional draw? (Fourth tranche) £

What is the number of months (from this Premium Collection point) to fourth tranche drawdown?

9.4 Sample Information Declaration

Lender organisation:	Little Tinkers
Business name:	XXXX Ltd
EFG/SFLG reference:	W5A39KG+01
Loan amount:	£100,000.00

System generated identification reference:	W5A39KG+01
What is the legal name of the Applicant business:	XXXX Ltd
What is the trading name of the Applicant if the Applicant trades under another business name?	N/A
What is the legal form of the Applicant?	Limited Company
What is the Applicant's Company Registration Number (if applicable)?	0123456
What is the current annual turnover of the Applicant?	£12,233,445.00
What is the Commencement of Trading Date of the Applicant business?	17-09-1961
What is the post code of the Applicant's main business address? (In instances where the Applicant's postcode is not available please enter the lender's branch postcode)	S3 8NH
What is the value of the EFG facility being applied for?	£00,000.00
Over what term does the Applicant intend want to repay the facility?	10 years
At what frequency will the Applicant make repayments of the principal of the facility? (Note: Type E, F, G & H facilities should be input as Interest Only unless there is to be a structured repayment of the facility principal over the period the guarantee is to be in place.)	Monthly
What Standard Industrial Classification (SIC) code best describes the business sector in which the guarantees facility will be used?	16240
SIC code activity description:	Manufacture of wooden containers

Which EFG Lending Type most accurately describes the facility to be guaranteed:	Type A – New Term Loan with no security
What is the principal purpose that this facility will be used for?	Research & Development
Including this facility, will the total outstanding balances and/or available facility limits of the Applicant's current EFG facilities be no more than £1.2m?	Yes
Value of De Minimis State Aid applicable to this facility (in Euro):	€14,773.57
Is the total value of the Applicant's De Minimis State Aid for the last three years (including that arising from this application) no more than €200,000?	Yes

To be completed by the Borrower

I/we confirm to the Lender and Government that:

- all the answers I have given here are true and accurate
- I have not left any information out
- information in all other documents I may have given you is true and accurate
- I understand that, even though the Government is providing a guarantee to the Lender in connection with my loan, I remain responsible to the Lender, for the loan and, in the event that I default on the terms of the loan (for example, by failing to make the specified repayments), the Lender is entitled to seek to recover the full amount outstanding from me

IMPORTANT: The information contained in this document is the formal record upon which decisions have been made. If any of the information contained in this declaration is incorrect the loan must be cancelled and a new application submitted. This document cannot be altered.

Signed ______________________________

Print name ______________________________

Position ______________________________

Date ______________________________

Signed ______________________________

Print name ______________________________

Position ______________________________

Date ______________________________

Signed ______________________________

Print name ______________________________

Position ______________________________

Date ______________________________

Signed ______________________________

Print name ______________________________

Position ______________________________

Date ______________________________

Signatories to be the same as those persons who are required to sign the Lender's Scheme Facility Letter.

9.5 Notes on Industrial Sector Restrictions

The Enterprise Finance Guarantee (EFG) is subject to sector restrictions arising from the EU *de minimis* State Aid rules, the Industrial Development Act 1982 (which provides the statutory basis for EFG) and also other national policy decisions.

Since the start of the EFG in January 2009, and in light of changes to the *de minimis* rules, certain sector restrictions have been lifted to ensure that EFG is available to as many viable businesses as possible. These are listed below along with those sectors where partial or full restrictions remain.

Overview of restrictions lifted

- Authors, music composers and certain other own-account artists
- Automotive
- Betting and gambling
- Commission agents
- Medical and health services (private & independent sector)
- Owning and dealing in real estate
- Postal and courier services (except the Post Office)
- Professional sports players and sporting organisations
- Shipbuilders
- Synthetic fibres
- Steel
- Ticket agents
- Tied public houses
- Veterinary services
- In addition, there is no specific restriction preventing EFG lending to charities.

Overview of remaining restrictions and the operation of the *de minimis* limit

The following restrictions, described in more detail below, arise from the EU *de minimis* regulations:

- Aid for Export
- Using EFG funding abroad
- Preferential use of domestic over imported goods
- Agriculture (including horticulture)
- Coal
- Fisheries
- Forestry
- Transport

For eligible cases, as the EFG guarantee has made the difference between failure and success in accessing finance, there is deemed to have been assistance from the Government to the business, generally referred to as “State Aid”. Like most forms of SME assistance, EFG operates under the *de minimis* rules which specify that the maximum assistance which may be provided to any SME in any rolling three-year period is €200,000 in grant aid, although lower thresholds apply in certain sectors.

To enable the *de minimis* State Aid received via each EFG loan to be easily aggregated on a ‘like-for-like’ basis with the value of any other such assistance an SME may have received, a ‘grant equivalent’ figure is calculated for the benefit arising from each guaranteed loan. The grant equivalent figure is calculated individually taking into account the loan value, loan term, repayments profile and a risk factor informed by the overall performance of the EFG-backed facilities, although in most cases the grant equivalent will not exceed 20% of the value of the loan.

In some cases, especially where the Borrower has had previous *de minimis* State Aid from other sources within the preceding three years, the value of the guaranteed lending permissible from a State Aid perspective may be less than either the EFG maximum of £1.2m or the Borrower’s desired amount. Similarly, receiving an EFG-backed loan will limit the value of other *de minimis* State Aid that the Borrower may receive over the next three years. In the event that a business knowingly makes a false declaration of previous *de minimis* State Aid the guarantee could be withdrawn from the Lender, which, in turn, could lead to the Lender seeking immediate repayment from the Borrower.

The Industrial Development Act 1982 precludes the use of EFG to assist or acquire banks and insurance companies.

The remaining restrictions exist for national policy reasons, primarily where the Government is already the main provider of, or source of funding for, these activities, where the activity adds little or no value to the business, or where activities of a similar type are also restricted.

Aid for Export, using EFG funding abroad, and the preferential use of domestic over imported goods

- Aid to export-related activities towards third countries or Member States, namely aid directly linked to the quantities exported, to the establishment and operation of a distribution network or to other current expenditure linked to export activity is ineligible for EFG.

- Aid that is contingent upon the use of domestic over imported goods is also ineligible for EFG.
- However, this restriction relates primarily to the purpose for which the loan is sought rather than the activities of the business, therefore, companies that happen to export as part of their business may be eligible for EFG.

Agriculture (including horticulture)

1) Activities related to primary agricultural production are eligible for EFG but with a maximum 'grant equivalent' value of €15,000, assessed individually. The corresponding equivalent maximum loan values are approximately £90,000 for loans of 5 years and £45,000 for loans of 10 years. Higher value loans for shorter terms will be possible subject to the State Aid value not exceeding €15,000.

Exception:

- When the amount of aid is fixed on the basis of the price or quantity of products put on the market.

2) Loans for the processing and marketing of agricultural products (beyond simply preparation for sale and packaging) are eligible for EFG.

Exceptions:

- When the amount of the aid is fixed on the basis of the price or quantity of such products purchased from primary producers or put on the market by the undertakings concerned.
- When the aid is conditional on being partly or entirely passed on to primary producers.

Banking, finance and associated services

- Any activity that involves a decision on and / or granting of finance to clients, such as banks, deposit takers and building societies; companies involved in granting loans, mortgages, hire purchase or credit services; mortgage brokers that are attached to banks; venture capitalists; seed corn finance companies and stockbrokers is not eligible for EFG.
- Accountants, auditors, management service companies such as bookkeeping firms, tax advisers, management consultants, business advisers and companies that provide services to small firms on financial matters without actually supplying funds, including financial advisors and

mortgage brokers, who are independent of banks and insurance companies, are eligible for EFG.

Business, employer & professional, religious and political membership organisations and trade unions

- Activities of business, employer and professional, religious and political membership organisations and trade unions are not eligible for EFG.

Coal

- This sector is specifically excluded from the *de minimis* rules and is, therefore, ineligible for EFG.

Education

- Formal education is excluded.
- Businesses offering courses that lead to vocational qualifications and skills (i.e. those skills and qualifications directly usable in a job) are eligible, as are nursery schools, day schools and playgroups for young children and sports coaching.

Extraterritorial organisations and bodies

- Activities of extraterritorial organisations and bodies are not eligible for EFG.

Fisheries

Activities related to the production, processing and marketing of fisheries products are eligible for EFG but with a maximum 'grant equivalent' value of €30,000, assessed individually. The corresponding equivalent maximum loan values are approximately £180,000 for loans of 5 years and £90,000 for loans of 10 years. Higher value loans for shorter terms will be possible subject to the State Aid value not exceeding €30,000.

Exceptions – when the aid:

- Amount is fixed on the basis of price or quantity of products put on the market.
- Increases fishing capacity, expressed in terms of tonnage or power, unless it concerns aid for modernisation and improving safety standards.
- Is for the purchase or construction of fishing vessels.

Forestry

- Forestry, as defined by EU guidelines, is the production of standing timber as well as the extraction and gathering of wild growing forest materials including products which undergo little processing, such as wood for fuel and industrial use.
- Activities aimed at directly contributing to maintaining and restoring the ecological, protective and recreational function of forests, biodiversity and healthy forest ecosystems may now be eligible for EFG subject to the relevant EU guidelines.

Insurance and associated services

- Insurance companies and any companies attached to insurance companies are not eligible for EFG.
- Insurance agents and brokers that do not provide insurance themselves and that are independent of insurance companies are eligible for EFG.

The Post Office (Royal Mail)

- Post Office branches which are directly managed by Post Office Ltd are not eligible for EFG.
- However, operators of branches which are managed on an agency or franchise basis may be eligible for an EFG backed loan, subject to satisfying an approved EFG Lender's commercial criteria as with any other EFG loan.

Public administration, national defence and compulsory social security

- Publicly (state) owned bodies and companies are largely ineligible, mainly due to the turnover limit associated with the UK SME Test.
- The defence sector is eligible, except where state owned.
- Compulsory social security relates to social security activities.

Transport

- Rail, water and air transport are eligible for EFG.
- Road transport sector is eligible, but with restrictions:

The road freight and passenger sector is eligible but with a maximum 'grant equivalent' threshold of €100,000, assessed individually but generally equating to a maximum loan value of around £650,000. Note that there is also a full prohibition on haulage firms using any EFG funds to purchase new haulage vehicles (however, it is permissible for a non-haulage firm to use EFG to purchase a haulage vehicle, as haulage is not its primary business activity). The corresponding equivalent maximum loan values are approximately £600,000 for loans of 5 years and £300,000 for loans of 10 years. Higher value loans for shorter terms will be possible subject to the State Aid value being no more than €100,000.

- The acquisition of road freight transport vehicles by businesses undertaking road freight transport for hire or reward is excluded.