

Guidance to SMEs Applying for Credit from Banks

1. Introduction

According to recent surveys commissioned by the Department of Finance, SME supply and demand for credit in Ireland has changed considerably in recent times. Demand remains muted as businesses adjust to lower levels of business and economic activity, while sources of supply have reduced. In addition, reduced or impaired collateral/security values and balance sheet distress from property exposures and lower business turnover are exacerbating this situation.

It is important therefore for SMEs to make the best possible case when applying for credit from financial institutions. Banks assess each business application for credit on a case-by-case basis and on its own merits and make decisions to approve the finance within the parameters of their respective credit policies.

This Guidance Helpsheet seeks to provide some practical information that will assist SMEs in accessing credit from the banks.

2. Applying for Credit

Having assessed all funding options open to your business and decided that you wish to formally apply for credit from a bank, the first step is to ensure that you can clearly demonstrate a thorough understanding of your business and its current and future financial position. It is also essential to ensure that all the relevant documentation, accounts and projections are ready and accurate.

- For established small businesses, you should meet and go through the business plan and application with your accountant and/or financial adviser.
- Smaller businesses such as microenterprises, sole traders or start-ups may not have access or funding to pay for financial advice, and should seek advice or assistance from their trade bodies or government agencies such as county enterprise boards or the soon to be established local enterprise offices.

It is critical that you prepare the '*right*' documents and information for your bank. This is the key documentation that will be required by the bank in considering your application.

Table 1: Documents and Information

| Documents | Description |
|--|---|
| An up to date Business Plan or proposal | The banking and accounting trade bodies have jointly developed a <i>Business Plan Guidance</i> helpsheet which will ensure a strong business plan can be developed. |
| Financial Information / Projections | This should include (where available) <ul style="list-style-type: none"> • Auditors statements for the previous 3 year trading period or appropriate annual financial statements • Up to date management accounts and cash flow statements to reflect the current trading period • Up to date aged list of creditors and debtors • Financial and cash flow projections for minimum of 1 year period and underlying assumptions but ideally for period for which funding is sought • Details of all sources of funding. This information is critical. The bank will need to see what proportion of funding will be provided by the borrower. Normally around 30% is usually required. |
| Tax Clearance Certificate | |
| Up to date Asset/Liability profile of the business and owner(s)/promoter(s) | This should describe the assets; their original cost and their current value as well as any borrowings and income from these assets. The Bank will also want to understand the backgrounds and experience of the principals involved in the business. |
| Collateral or Security | Details of the proposed collateral/security available to support the credit request |

Normally, you will have a dedicated Relationship Manager at the branch. You should arrange to meet him/her in order to complete the Standardised Business Lending Application Form.¹ At the meeting the Relationship Manager will inform you if the bank has any additional requirements in relation to supporting documentation and information.

The IBF has developed a Standard Small Business Credit Application Guidance which is available at <http://bit.ly/IBFSMEapplication>. This general guidance on the completion of credit application forms includes specific guidance for credit applicants in the hotels/leisure and farm business sectors.

At the branch your relationship manager is the person who typically makes your case to a centralized credit committee that decides whether to lend or not. It is critical that the

¹ Bank of Ireland SME Business Lending Application Form available at http://www.bankofireland.com/fs/doc/wysiwyg/D3544_BOI_Business_Lending_App_Form_SEPT_2011_ELECTRONIC_VERSION_2.pdf;
AIB SME Business Lending Application Form available at <http://business.aib.ie/site-files/docs/products/finance-and-loans/AIB%20SME%20Application%20Form%20-%202006-10-2011v3%20FINAL%20editable%20version.pdf>

relationship manager really understand your business. This is why a well written application supporting the discussion you have with your Relationship Manager is so important as it can be used for reference when he/she is making the case internally.

3. Business Plan

As indicated above it is essential that you have developed an up to date business plan or proposal that is appropriate to the scale to your business and credit requirements – a simple microenterprise will require a simple business case; a larger more complex business will require a more extensive business plan and projections.

The discipline of preparing a structured business plan will also assist business owners and promoters in developing clear business strategies and demonstrating their knowledge and understanding of their business. It is important for you, the promoter, to take real ownership of the business plan on an ongoing basis, and not to view it as a procedural exercise to satisfy the bank.

The CCABI² and the IBF³ Business Plan Guidance helpsheet has been designed to facilitate the use of a common approach, framework and language in the preparation of business plans and the raising of bank finance. This document is available at; http://www.ibf.ie/Libraries/Guides_Forms/CCABI_IBF_Business_Plan_Guidance_2012.sflb.ashx.

Table 2 below lists the main headings that should be used as the skeleton for the business plan.

Table 2: Business Plan Key Headings

| | | |
|--|-----------------------------|--|
| 1. Name of business and contact details | 6. Staff details – optional | 11. Business risks and responses to risk |
| 2. Executive Summary | 7. Legal Status | 12. The project – optional |
| 3. Business owners and/or directors | 8. Names of advisers | 13. Request for finance |
| 4. The Business | 9. Suppliers – optional | 14. Financial Information |
| 5. Products, services, customers and marketing | 10. Business assets | |

² Consultative Committee of Accountancy Bodies Ireland

³ Irish Banking Federation

4. Credit Declines and Withdrawals

In circumstances where an application for credit is declined, the lender must, under the Central Bank's Code of Conduct for Business Lending to Small and Medium Enterprises, explain clearly to the SME why the application was declined.

Applicants may seek a review of the decision to decline an application for credit or to withdraw an existing credit facility through the bank's internal appeals procedures.

Small business and farm enterprise who have applied to banks that have engaged with the NAMA may also apply to the Credit Review Office, which reports to the Minister for Finance. The Credit Review Office provides an independent assessment of the viability of the lending application. For more details on the Credit Review Office, including eligibility criteria and how to apply, please visit the Credit Review Office website at <http://www.creditreview.ie/>.

5. Restructuring Your Finances

If there is a need to refinance or restructure existing debt, a key to success is to discuss it with your bank as early as possible. In order to ensure the best case is made, SMEs should not only work with their accountant and/or adviser, but also seek advice from the broad network of state agencies and industry bodies that provide supports to SMEs (see table 3). As is outlined in Section 6, the Code of Conduct for Business Lending to Small and Medium Enterprises was revised to specifically assist borrowers and lenders to address financial difficulties.

Although each SME, seeking to restructure their finances, needs to be considered on a case by case basis, SMEs should explore the full range of options that may be available from their bank including short-term forbearance and medium term forbearance measures and where appropriate more fundamental restructuring arrangements.

One of the consequences of the dramatic collapse in the property market is that there is a significant grouping of 'challenged' SMEs where the core business is viable but the enterprise is weighed down or constrained by debt overhang related in particular to property exposures.

These challenged, but still viable SMEs while continuing to trade are not transitioning to a situation where they can begin to progressively tackle the property debt that is indirectly linked to their business.

In such circumstances it is critical that there is active and positive engagement between the SME and their bank in which there is a clear focus on developing a practical solution that meets the needs of both parties. In instances where SMEs financial problems are temporary, what may be required is some form of short-term forbearance — for example suspension of capital payments to improve cost flows within the business. Equally, the SME may seek to use this period to implement new measures designed to improve their

financial situation for example introducing a cost cutting programme and/or initiating a new sales drive.

Where, however, such traditional forbearance measures are insufficient what may be required is a more sophisticated strategy involving more medium-term forbearance initiatives. This would be designed to establish the viability of the core business, identify the company's sustainable direct debt and ultimately disentangle indirect debt.

A positive working relationship between the SME and the bank in which both parties are aware of their rights and responsibilities is vital to this workability of this type of approach to SME arrears. In circumstances where the SME is particularly over borrowed, ensuring the sustainability of the business may actually require a transitioning to a more fundamental restructuring arrangement. This could involve some form of performance related restructuring based on adherence to the alternative repayment arrangement.

6. Financial Difficulties: the Central Bank of Ireland's Code of Conduct for Business Lending to Small and Medium Enterprises

In January 2012 the Central Bank of Ireland issued its revised statutory Code of Conduct for Business Lending to Small and Medium Enterprises, which sets out new requirements for lenders — including banks — when dealing with SMEs in, or facing, financial difficulties. The revised requirements establish a clearer framework that is designed to assist SMEs and lenders to work together to address existing or emerging arrears situations and financial difficulties.

The Code reaffirms that each SME needs to be considered on a case by case basis and that it is important for SMEs at risk of going into arrears to contact their lender early to inform them of the difficulties in order to discuss mechanisms to address the situation.

The revised Code sets out the basic entitlements that an SME in financial difficulties should expect when engaging with their bank including:

- A lender must provide SMEs with an information booklet setting out the procedure for dealing with financial difficulties cases including timeframes and the implications for the SME.
- A lender must provide an SME with the list of information required in order to assess the SME for a possible alternative repayment arrangement.
- The SME should receive a response from the lender in relation to its decision on a repayment arrangement within 15 business days of the lender having received all the necessary information.

- The SME must be informed by the lender of its right to appeal the lender's decision on the repayment arrangement.
- Where an SME is concerned about meeting repayments and approaches the lender, the SME must be offered an immediate review meeting to discuss their circumstances and assess the potential for the SME to be offered an alternative repayment arrangement.

The revised Code is available on the Central Bank's website at <http://www.centralbank.ie/Pages/home.aspx>.

7. Supports for SMEs

The table below provides details of broad range of state agencies and industry bodies that have a role in providing supports and/or advice to SMEs.

Table 3: State Bodies and Industry Groupings providing Supports and Advice for SMEs

| Departments, State Agencies and Statutory Bodies | |
|---|--|
| Organisation | Website |
| Department of Jobs, Enterprise and Innovation | www.enterprise.gov.ie/ |
| Enterprise Ireland | www.enterprise-ireland.com/en/ |
| County and City Enterprise Boards | www.enterpriseboards.ie/index.aspx |
| Bord Bia | www.bordbia.ie/Pages/Default.aspx |
| Bord Iascaigh Mhara | www.bim.ie/ |
| SEAI (Sustainable Energy Authority Ireland) | www.seai.ie/Home/ |
| Udarás na Gaeltachta | www.udaras.ie/ |
| Western Development Commission | www.wdc.ie/ |
| Central Bank Ireland | www.centralbank.ie/ |
| Fáilte Ireland | www.failteireland.ie/ |
| Leader Partnerships | www.leaderpartnership.ie/ |
| Culture Ireland | www.cultureireland.ie/ |
| Irish Film Board | www.irishfilmboard.ie/ |
| Credit Review Office | www.creditreview.ie |
| Department of Social Protection | www.selfemployedsupports.ie/ |

| Industry and Representative Bodies | |
|---|--|
| Organisation | Website |
| Small Firms Association (SFA) | www.sfa.ie |
| Irish Small and Medium Enterprises Association (ISME) | www.isme.ie |
| Chambers Ireland (and affiliated chambers) | www.chambers.ie |
| Irish Farmers Association | www.ifa.ie |
| Irish Banking Federation | www.ibf.ie |
| Small Business Finance | www.smallbusinessfinance.ie/ |
| CCAB-I (Consultative Committee of Accountancy Bodies Ireland) | www.ccab-i.ie/ |
| Irish Hotel Federation | www.ihf.ie/ |
| IntertradeIreland | www.intertradeireland.com/ |