

Preparing for Loan Underwriting and Examining Your Loan Agreement

As a business owner who may be considering debt financing, your ultimate goals are a) to get your loan approved, and b) to make the right decision for you and your business when reviewing the loan offer. If your loan application is really strong, you could even end up with multiple offers. If this is the case, you'll still need to assess which offer is the right one for you.

Here are some things you can do to improve your chances of achieving these goals:

- ✓ Be proactive and organize the information needed for the loan underwriting process.
- ✓ Familiarize yourself with the fundamental components of a loan agreement.
- ✓ Do your homework to select the funder that is the best fit for you and your business.

This way, when you are at the point where you're reviewing loan packages, you have what you need to make an informed decision.

With these goals and strategies in mind, use the information in **Part 1** to practice organizing the necessary information for the loan underwriting process. In **Part 2**, examine the components of a loan agreement.

PART 1 | Organize Your Information and Documents: Kickstart the Loan Underwriting Process

Let's say that after exploring a few funding options—friends and family, credit unions, commercial finance companies, banks and so on—you've identified a funding source and are ready to apply for a loan and engage in the underwriting process. Loan underwriting simply refers to a process that lenders use to evaluate your loan application and determine whether or not they'll approve your loan. Your job is to organize your information to show them that you are a good fit.

Put yourself in the lender's shoes for a moment. What expectations would you have from someone to whom you're lending money? It would be to get your money back, including the interest, and get it back on time. To assess if you'll meet this expectation, lenders typically look at the 5 C's of your credit: capacity, capital, conditions, collateral and character.

Tip: If you haven't done so already, check out *Explore Your Debt Funding Options* a) for more on identifying the right funding source for your business needs and b) to know more about the 5 C's of credit.

Business loan requirements may vary from lender to lender. But if you can organize and gather the following information and documents, it will help address the overarching concern: Will you repay the loan? Organizing the information below can also help speed up the loan process for your business.

- **A statement of purpose/executive summary:** Craft a well-written and informative executive summary.¹ The checklist below will help you put together this summary.
 - **Purpose:** Describe how you plan to use the loan and how it will have a positive impact on your business.
 - **Amount:** Specify the loan amount you need. Show that your business needs align with the loan amount you're requesting. (See the Business Plan section below.)
 - **Maturity:** Specify the duration for which you need the loan.
 - **Repayment:** Clearly explain, with documentation, how you/your business plan to repay the loan. (See the Financial Documents section below.)
 - **Collateral:** Show that your business is low risk. Identify available collateral—real estate, vehicles, equipment, etc.—along with its estimated worth.
 - **Business description:** Give the lender a peek into what your business does. Check out this [example](#) of an executive summary for a loan request.
- **Business plan:** Include a compelling business plan that tells the story of your business and your plans for its future. Showcase your company—why your business exists (vision), core team and their key expertise, number of employees, products and services you offer, key facilities and suppliers, and marketing and distribution. Be sure to clearly show how you intend to grow, and include your current and projected financial statements.

If you don't have a business plan or are looking to polish an existing one, check out this business plan [template](#).

- **Financial documents:** The checklist below will help you gather the necessary financial documents.
 - **Cash flow statement:** Show that your business is generating enough money to repay the loan. Check out these templates for 12-month and three-year cash flow statements:
 - [12-month Template](#)
 - [3-year Template](#)
 - **Balance sheet:** Show your business's net worth at a specific point in time.² Need a template to put together a balance sheet? Check out this [resource](#).
 - **Income statement** (also called the statement of profit and loss): Show how your business has performed over a given period—the amount of profit or loss generated.³ Banks generally like to see profit and loss statements for the last three years.
 - **Personal finance statement:** Show your net worth—your personal assets and debts—as a borrower. Need a template to put together your personal finance statement? Check out this [resource](#).

PART 2 | Examine Your Business Loan Agreement

A successful loan underwriting process, meaning the lender approves your loan, will result in the lender producing a loan agreement. But before signing, you need to make sure you understand and agree with the information in the loan agreement.

Although the components of a business loan agreement may vary from lender to lender, look out for the following essential components that are typically common across all loan agreements. Use this information to assess if the loan offer is right for you.

- **Loan amount:** Verify that the amount specified in the agreement is correct and matches what you agreed to borrow.
- **Interest rate:** Check the interest rate associated with your loan. If the lender considers you a high-risk borrower, then it's possible they'll set a high interest rate. Consider exploring other loan offers to see if another lender might offer a lower interest rate on your loan.
- **Type of interest rate:** Check the details for the type of interest you'll be paying: fixed, variable, floating, balloon, graduated, etc. For example, if you'll be paying variable interest, when will the interest rates change?
- **Fees:** Check what kinds of fees you may need to pay. For example, what will the penalties be for missed/late payments? Is there a grace period to make the payments?

- **Repayment schedule:** What's the payment schedule—daily, weekly, monthly, etc.—and how much will you be paying each time? Your payment schedule and loan duration will help you determine the total cost of your loan. For example, a 15-year loan will cost you more per month, but the total loan amount will be lower than the amount you'd pay on a 30-year loan.
- **Penalty for early payment:** Check if you'll be penalized for paying off your loan early. By paying early, you are able to pay a lower amount of interest; however, not all lenders allow this practice.
- **Collateral requirements:** Did you agree to secure your loan with collateral? If yes, then review the requirements around that—what personal and/or business items could the lender take ownership of if you're unable to repay the loan? Are you comfortable with these requirements?

Check out this [sample](#) business loan agreement, and explore its components.

TIPS

- If you're not comfortable with the terms and conditions—such as interest rates and personal guarantees—in your loan agreement, consider negotiating a better deal.

“In business loans, as in other business contracts, each situation is unique, and everything is negotiable. For example, your lender may want some specific covenants (guarantees) on the loan, or you may agree to a different way.”

—Jean Murray, Educator and Owner of Emence Enterprises LLC.⁴

Check out this [resource](#) for more on negotiating loan terms.

- If you're finding that the terms and conditions in your loan agreement seem too good to be true, then they probably are. If it's feasible, get with a trusted advisor and/or a lawyer to understand the details and fine print of the loan agreement and figure out if the agreement is credible.

RESOURCES

If you need guidance figuring out what types of debt funding you might qualify for and how to best present your loan request to lenders, contact the many [Small Business Development Centers](#) (SBDs) around the country.

¹ How to Prepare a Loan Package, <https://www.sba.gov/media/training/sbalp/index.htm> (accessed May 3, 2019).

² *Ibid.*

³ *Ibid.*

⁴ Jean Murray, *What Is Included in a Business Loan Agreement?* (Jan. 12, 2018) <https://www.thebalancesmb.com/what-is-included-in-a-business-loan-agreement-4157618>, (accessed May 3, 2019).