Lending Policies and Procedures
Factors Determining the Mix of Bank Loans

- Characteristics of Market Area
- Lender Size
- Experience and Expertise of Management
- Expected Yield of Each Type of Loan
- Regulations
Bank’s Written Loan Policy

- Goal Statement for Bank’s Loan Portfolio
- Specification of Lending Authority of Each Loan Officer and Committee
- Lines of Responsibility in Making Assignments and Reporting Information
- Operating Procedures for Soliciting, Evaluating and Making Loan Decisions
- Required Documentation for All Loans
- Lines of Authority for Maintaining and Reviewing Credit Files
Bank’s Written Loan Policy (cont.)

• Guidelines for Taking and Perfecting Collateral
• Procedures for Setting Loan Interest Rate
• Statement of Quality Standards for All Loans
• Statement of Upper Limit for Total Loans Outstanding
• Description of the Bank’s Principal Trade Area
• Procedures for Detecting, Analyzing and Working Out Problem Loans
Steps in the Lending Process

• Finding Prospective Loan Customers
• Evaluating a Customer’s Character and Sincerity of Purpose
• Making Site Visits and Evaluating a Customer’s Credit Record
• Evaluating a Customer’s Financial Record
• Assessing Possible Loan Collateral and Signing the Loan Agreement
• Monitoring Compliance with the Loan Agreement and Other Customer Service Needs
The Five Basic C’s of Lending

- **Character** – Specific Purpose of Loan and Serious Intent to Repay Loan
- **Capacity** – legal authority to sign binding contract and financial capability (future cash flows)
- **Capital** – equity investment by borrower
- **Conditions** – economic conditions faced by borrower
- **Collateral** – adequate assets to support the loan
Common Types of Loan Collateral

- Accounts Receivables
- Factoring
- Inventory
- Real Property
- Personal Property
- Personal Guarantees
Information About Consumers

- Consumer-Supplied Financial Statements
- Credit Bureau Reports
- Experience of Other Lenders
- Verification of Employment
- Verification of Property Ownership
- The Web
Information About Businesses

- Financial Reports Supplied by the Borrowing Firm
- Copies of Board of Director’s Resolutions or Partnership Agreements
- Credit Ratings – Dun & Bradstreet, Moody’s, Standard & Poor’s
- Risk Management Associates, Dun & Bradstreet Industry Averages
- Web
Information About Governments

• Government Budget Reports
• Credit Ratings Assigned to Government Borrowers By Moody’s, Standard & Poor’s, Fitch
• Web
Parts of a Typical Loan Agreement

- The Note
- Loan Commitment Agreement
- Collateral
- Covenants
  - Affirmative
  - Negative
- Borrower Guaranties and Warranties
- Events of Default
Loan Review

• Examination of Outstanding Loans to Make Sure Borrowers are Adhering to Their Credit Agreements and the Bank is Following Its Own Loan Policies
Loan Review Procedures

• Carrying Out Review of All Types of Loans on a Periodic Basis

• Structuring the Loan Process
  – Record of Borrower Payments
  – Quality and Condition of Collateral
  – Completeness of Loan Documentation
  – Evaluation of Borrower’s Financial Condition
  – Assessment as to Whether Fits with Lender’s Loan Policies
Loan Review Procedures (cont.)

- Reviewing Largest Loans Most Frequently
- Conducting More Frequent Reviews of Troubled Loans
- Accelerating the Loan Review Schedule if Economy or Industry Experiences Problems
Warning Signs of Problem Loans

- Unusual or Unexpected Delays in Receiving Financial Statements
- Any Sudden Changes in Accounting Methods
- Restructuring Debt or Eliminating Dividend Payments or Changes in Credit Rating
- Adverse Changes in the Price of Stock
- Losses in One or More Years
- Adverse Changes in Capital Structure
- Deviations in Actual Sales from Predictions
- Unexpected and Unexplained Changes in Deposits
Loan Workouts

The Process of Resolving a Troubled Loan So the Bank Can Recover Its Funds