

# Transamerica Small Business Capital Risk Management Conference

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*This document was originally prepared for a Transamerica Small Business Capital Risk Management Conference in Greenville, South Carolina on September 12-13, 2001.*

*As we sat in our conference room on the morning of September 11, preparing the final draft of this document, people began to interrupt our meeting saying, "Our country is under attack."*

*"I know this meeting is important," said one woman, "but some things are more important."*

*Each day since, we recognize that whatever risk we may find in our work is feeble compared to the sacrifice of those heroes in Washington, New York and Pennsylvania "who more than self their country loved, and mercy more than life."*



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## Conference Overview

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### Purpose

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The purpose of this conference is to introduce our people and our operations to ensure that, as TSBC progresses through the sale process:

- Transamerica is aware of the issues and risk factors in the SBA business,
- Transamerica adequately supports the business in a way that minimizes these risk factors and
- Transamerica is prepared to continue to manage the remaining assets and risk.

### Format

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The original design of the risk management conference included brief presentations from each of the TSBC senior managers, beginning with a summary presentation by the president, Scott Lining. After these presentations we would have had more detailed discussions of portfolio management risks, operational, legal and transition issues.

This document includes the support material for the presentations and a brief agenda for one of those additional discussions. Additional time-sensitive detail would have been provided separately.

To succinctly present the essential issues of TSBC's operation, assets and risk, each manager provided a one-page introduction to his or her department covering the following topics:

*People*

*Function*

*Accomplishments*

*Risk*

The president's summary includes a top-level brief for the entire company and the managers detail these topics for their departments. Some of the risk items are inherent in our business and assets; some derive from external conditions such as changes in SBA priorities; some inhere in the sale process itself. In some cases, the risk items are forward-looking as managers anticipate risk areas that could develop in the future, even though we are currently successful in managing these risks, as we describe in several of the accomplishments.

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# TSBC Overview

## *Scott Lining*

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### People

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- Diverse Backgrounds
- Experienced in SBA Operations
- High Achievers
- Marketable
- Principled

### Functions

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- Maintain a stable servicing operation to meet our obligations to our borrowers, our Parent company and SBA
- Guide the company through due diligence, sale and transition

### Accomplishments

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- Reorganized TSBC organizational structure to improve its effectiveness in servicing of the portfolio in 2001
- Prepared the company for due diligence activities and audits in 2001
- Obtained the highest rating on the SBA's PLP Examination (Preferred Lender Program)
- Obtained the highest ratings on the SBA's Safety and Soundness Examination
- Improved processes throughout Finance, Servicing and Liquidation
- Remittance Reconciliation Process
- Tickler System Overhaul
- Servicing Tracking System
- Liquidation Tracking System

### Risks

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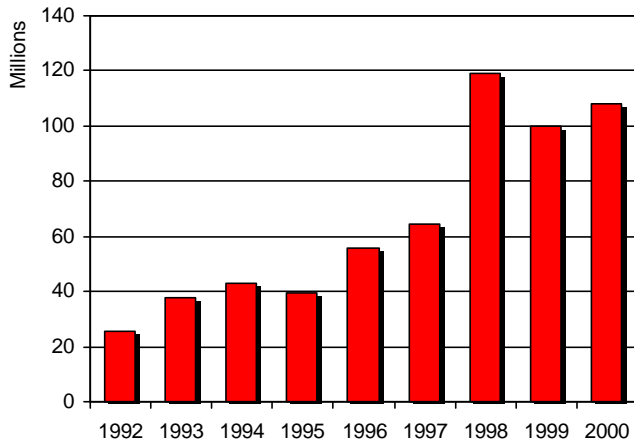
- Failure to service and liquidate loans in a prudent manner will result in higher delinquencies and losses to the company.
- Failure to act as a prudent lender in underwriting, closing, servicing or liquidation can jeopardize the SBA guaranty on a loan.
- Failure to maintain PLP servicing status would complicate the servicing and liquidation process resulting in higher operating costs, increased scrutiny by the SBA and possibly more frequent denials of the SBA guaranty
- Failure to retain qualified personnel could jeopardize the quality of the portfolio and PLP status and could adversely affect the sale of the assets.

## TSBC at a glance

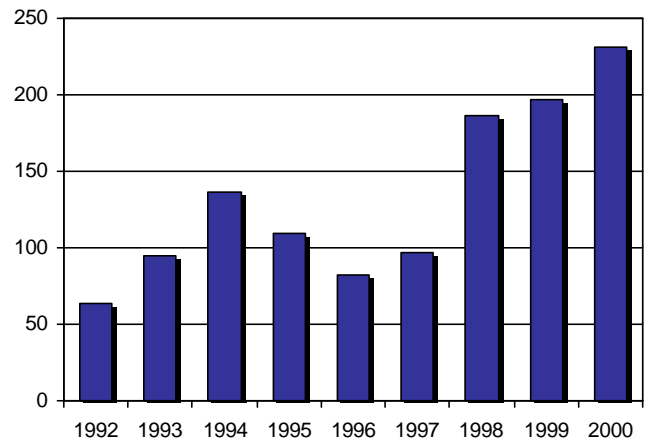
- December 1991      Incorporated as Emergent Business Capital through purchase of inactive SBLC license
- May 1995            Entered 504 loan program
- June 1995            First securitization
- September 1995    Achieved PLP certification
- November 1998    Purchased by Transamerica Business Credit Corporation
- December 1998    First year over \$100 Million in loan production

• Managed Receivables:.....	\$300 million
• Owned Receivables: .....	\$100 million
• Number of Loans: .....	700
• Average Loan Size: .....	\$450,000
• Wtd. Avg. Spread Over Prime: .....	2.20%
• Wtd. Avg. Servicing on Sold Loans:...	1.17%

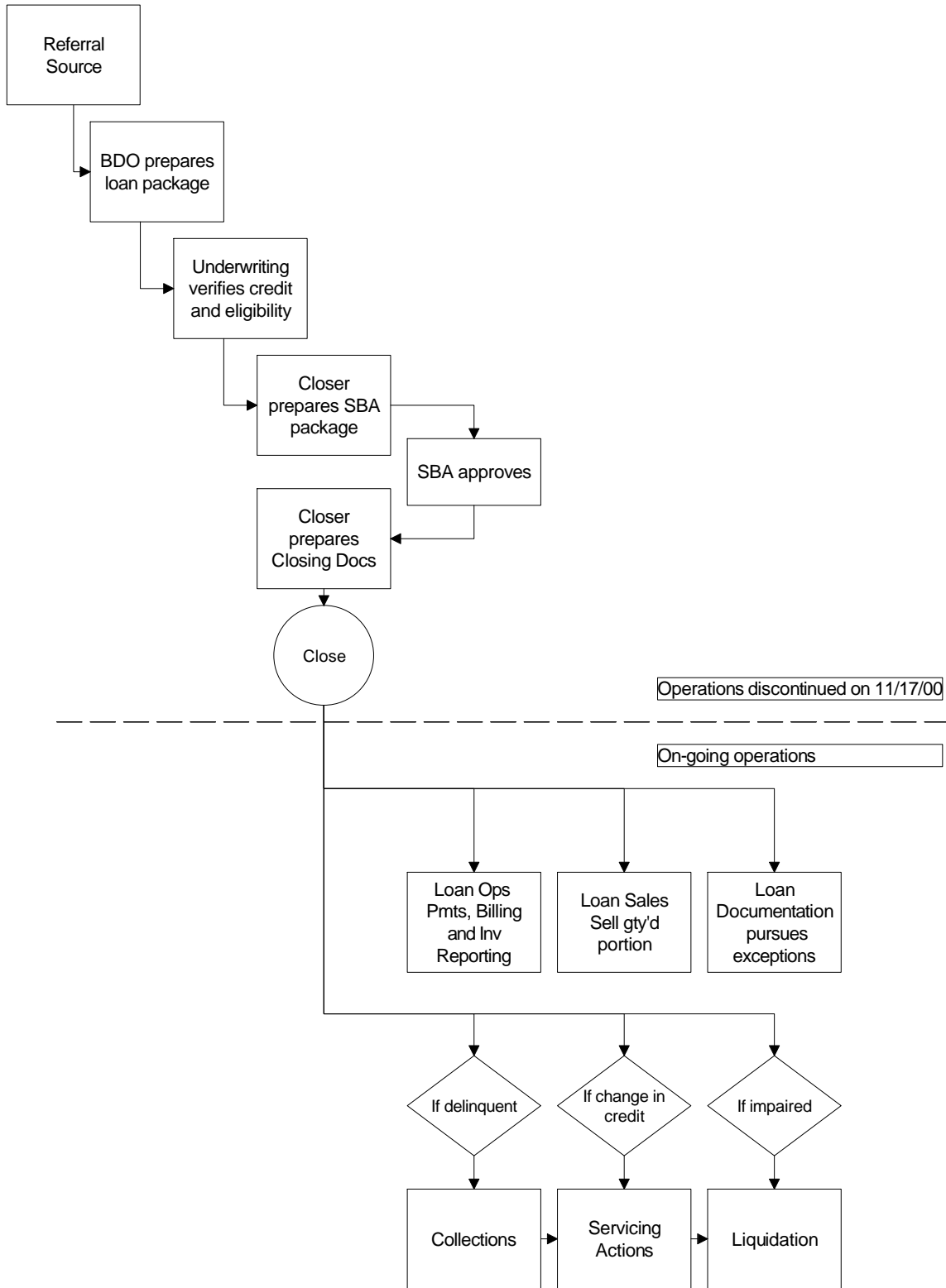
**Loan Volume in Dollars**



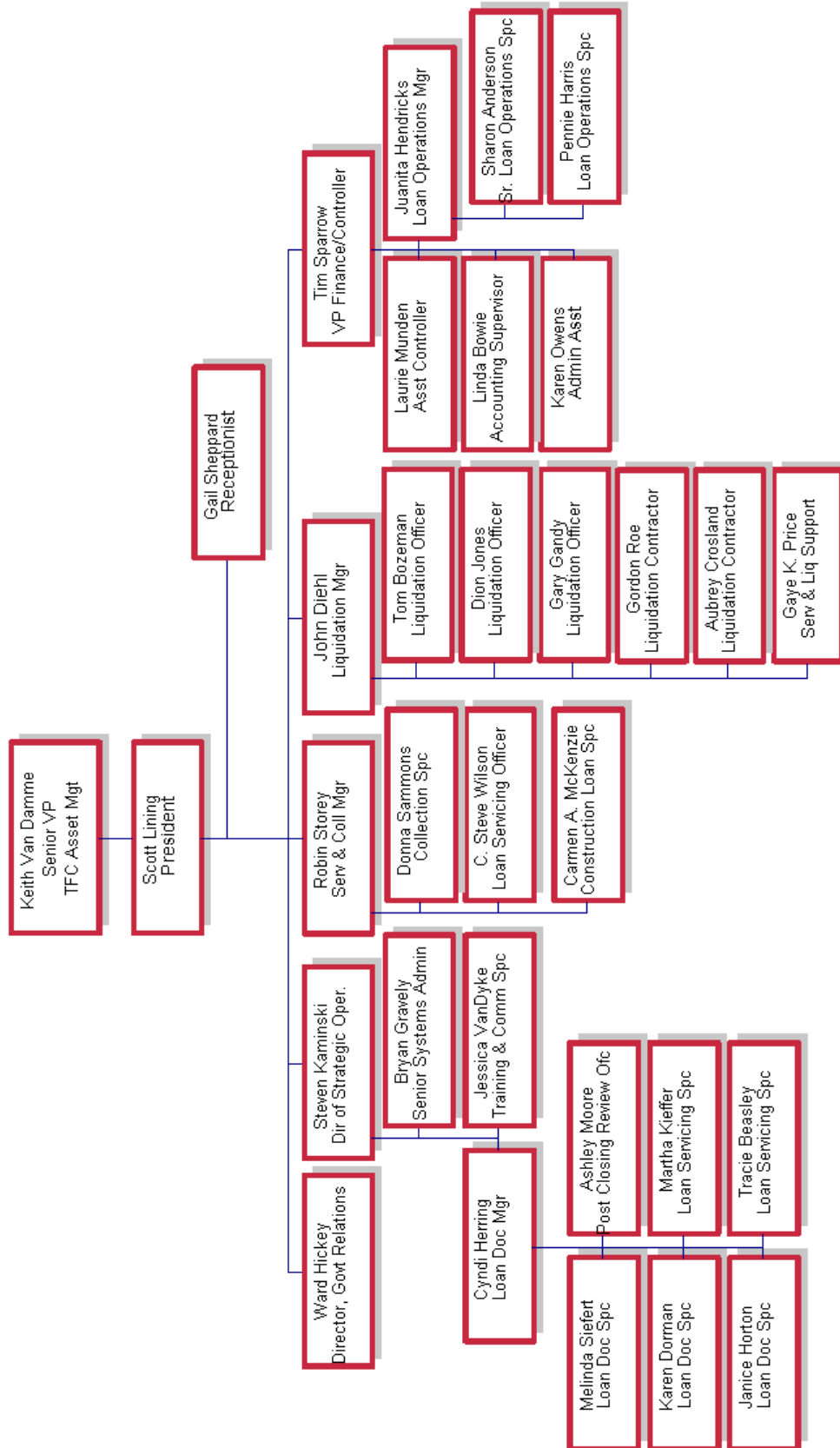
**Loan Volume in Number of Loans**



# TSBC Basic Workflow



# TSBC Organizational Chart



## Management Biographies

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- **A. Scott Lining:** President of TSBC since November, 2000. Formerly VP-Finance since 1997 and Controller since 1995 when he joined the company. Since 1995, Mr. Lining has managed the Finance and Loan Operations areas of the 7(a) and 504 companies, as well as other affiliated companies. Before coming to Emergent in 1995, he worked in the Accounting and Financial Reporting area of Advantica (a restaurant holding company) as well as in the Accounting department of one of its subsidiaries for a total of 4 years where his primary responsibilities included SEC reporting and bank covenant compliance. Mr. Lining obtained his accounting training at Deloitte & Touche where he worked for 4 years, two of them as a Senior Accountant responsible for managing audit engagements. He holds a Bachelor of Science degree from Bob Jones University and has been a Certified Public Accountant since 1989.
- **Robin L. Storey:** Vice President, Loan Servicing & Collection Manager. Joined Emergent Business Capital in 1997 as Senior Loan Officer of Asset Based Lending and transferred to SBA group as Production Center Manager in June 1998 due to sale of the Asset Based Lending group. Ms. Storey served as Regional Production Manager for TSBC from 1998-2000. She came to Emergent from First Capital Bank in Atlanta (1991-1997) where she was SVP, Senior Credit Officer. Ms. Storey holds a BBA in Management from Georgia State University and is a graduate of the Graduate School of Banking of the South at LSU, and has 17 years of commercial lending experience in Asset Based Lending, Construction Lending, SBA Lending and Consumer Lending.
- **John G. Diehl:** Vice President, Liquidation Manager. Joined Emergent Business Capital, Inc. June 1998 as liquidation officer, prior to the acquisition of Emergent by TSBC November 1998 and became Loan Servicing, Collection and Liquidation Manager in December 1998. Mr. Diehl joined TSBC from SunTrust Bank Atlanta, where he managed the loan servicing department of their strategic partner (franchise, distributor) lending division 1997-1998. He was previously employed by Norwest Bank Minnesota 1985-1997 as commercial loan workout officer/team leader and commercial lending officer. Mr. Diehl has over 20 years experience in commercial lending. He earned a BS from the University of Wisconsin, Oshkosh.
- **Tim Sparrow:** Vice President of Finance. Joined Emergent Business Capital as Assistant Controller in March 1998. Mr. Sparrow served as Controller from late 1999 to 2001 when he was appointed to his present position. Prior to joining Emergent, Mr. Sparrow worked as a public accountant. He holds an MBA from Clemson University, designations as Certified Management Accountant and Certified in Financial Management and is licensed as a Certified Public Accountant in the state of South Carolina.

- **Steven H. Kaminski:** Executive Vice President, Director of Strategic Operations. Directs resource utilization and management planning. He also served as Director of Communication, Change Manager and IT Manager. He joined TSBC in 1996 working initially on process definition and the development of a loan origination system, later moving to technology management and directing various internal change programs. Dr. Kaminski has also developed sales force automation and business-to-business e-commerce relationships. He holds a Bachelor of Arts degree, a Master of Arts degree, a Master of Fine Arts degree and a Ph.D. in Communication from The Ohio State University, earned in 1995.
- **Juanita Hendricks:** Loan Operations/Loan Accounting Manager for TSBC since January 1997. Current duties include overall responsibility of the Loan Accounting System, development and enforcement of Loan Operations controls and procedures, customer service and support to Accounting, Loan Servicing and Liquidations. Prior to TSBC, Ms. Hendricks was Senior Financial Analyst for American Federal Bank (currently CCB) 1987 to 1997, where her duties emphasized FHLB reporting, Secondary Market accounting and reporting, and Troubled Debt (foreclosures, workouts, investigative work, etc.). She holds a B.S. in Accounting from Clemson University and various certifications including specific loan accounting systems and SBA reporting.
- **Cyndi Herring:** Vice President, Loan Documentation and Loan Sales. Having joined TSBC in 1992, currently directs the loan documentation unit and secondary market loan sales. Ms. Herring has also served as the National Loan Closing Manager and as a Loan Servicing Officer. Having previously worked as a SBA Loan Manager at Regions Bank and as Loan Auditor at First Union, she has almost 20 years of experience in commercial lending. Ms. Herring attended Rutledge Business College.
- **Howard J. Hickey, Jr.:** Senior Vice-President and Director of Government Relations. Mr. Hickey joined TSBC in May, 1999 as eastern origination manager of credit products and moved to his current position at the start of 2000. He maintains working relationships with SBA district directors for government guaranteed credit products in all 10 SBA regions and has functional secondary market operational expertise. Mr. Hickey brings over 20 years of Money Center commercial banking experience, recently serving as North East and South West Regional Manager of Bank of America, FSB, California; SVP and Senior Credit Officer at FIB, New Mexico and Director of Priority Lending for BankOne in Arizona. He was Principal of Hickey LTD., a RIA and licensed RTC Contract Agent for Servicing & Liquidation of Commercial and Real Estate Loans in AZ and NM. Hickey holds a Bachelor's degree from Fairfield University, a Master's degree from Springfield College; and is a graduate of Columbia University Banking School in New York and the Duke University Executive Program in North Carolina. He was inducted into the National Honor Society at Springfield College.

## Significant organizational changes since March, 2000

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### **Aegon Decision to Exit SBA Business, March, 2000**

- March, 2000, Aegon NV, parent of Transamerica, announced its intention to sell its entire commercial finance unit as a whole, of which TSBC is a part, choosing to keep the insurance companies.
- March 1, 2000 Aegon announced a retention package for all employees to maintain the stability of these units during the sale.
- July, 2000, Aegon announced that because no suitable buyers came forward, it would keep the commercial finance companies as a whole, but review individual units for a possible sale.
- November 1, 2000, Aegon NV completed a strategic review of Transamerica Finance Corporation and decided to make opportunistic divestments of certain non-core commercial finance units, including Transamerica Small Business Capital.
- Morgan Stanley Dean Witter retained to assist Aegon in a possible SBLC asset or business unit sale.

### **Production Shutdown, November, 2000**

- As part of this sale process, TSBC ceased origination of all new loans on Friday, November 17, 2000 in order to focus on the sale of the loan portfolio.
- November 17, 2000, Scott Lining assumes role of President.
- TSBC phased out our production resources over the next several weeks.
  - On November 28, 2000, TSBC released all sales and some production staff, keeping all servicing, liquidation and portfolio management personnel and those needed to support them.
  - Some members of production staff are retained to assist in office closings, PLP audit preparation and disposition of loans remaining in production.
  - December 31, 2000, final loans in production are closed.
  - February 28, 2001, after completion of PLP audit, final production staff members outside Greenville are released. Only one employee outside Greenville remains.
- November 30, 2000, TSBC senior management visited SBA in Washington to discuss details of the production shutdown, sale plans and to address any SBA concerns.
- Portfolio management operations continue to service and liquidate all loans at our Greenville, SC, headquarters, using prudent lending practices in compliance with the SBA's standard operating procedures.

**Reorganization, January, 2001**

- Liquidation and Servicing are split between two separate managers to better utilize existing personnel. John Diehl serves as liquidation manager. Robin Storey is the servicing manager.
- Loan Documentation team is formed to complete documentation audits, clear documentation exceptions and maintain ongoing loan documentation.
- The servicing, liquidation and loan documentation staff is augmented by reassigning qualified production personnel after new originations shutdown.
- Dedicated high-level administrative support assigned to liquidation staff.
- Additional liquidation staff is hired in May, 2001 to process additional liquidation accounts.
- Current organizational structure consists of the following departments: servicing, liquidation, loan operations, loan documentation, finance and servicing support (admin, IT).
- The same support services are still performed by the parent company: tax, treasury, human resources and payroll.
- July, 2001, TSBC began to report to the Senior Vice President of Transamerica Finance Company in charge of Asset Management.

**Process Changes, March, 2001**

- Soon after the reorganization, TSBC began several initiatives to improve the quality and consistency of ongoing operations. These efforts included:
  - Rebuilding the electronic tickler system.
  - Clarifying file handling and maintenance procedures.
  - Clarifying procedures for insurance follow-up and UCC continuations.
  - More consistent procedures to obtain and review of borrower financial statements and tax returns.
  - Establishing more consistent management oversight of liquidation and servicing tasks.
  - Involving servicing officers sooner in collection efforts.
  - Distributing servicing workload by geographic regions.
  - Developed interface between loan accounting system and ancillary systems that track servicing, liquidation and loan documentation activities.
  - Automating processing of servicing actions and status changes.
  - Detailed tracking of all servicing actions.
  - Began development of system to track and prioritize liquidation activities.

**Sale Progress, February, 2001 to present**

- Prospective buyers began due diligence in February, 2001.
- One possible sale was aborted in May, 2001.
- Aegon/Transamerica is currently in discussions with other potential buyers regarding the purchase of all or part of the portfolio.
- TSBC management continues to pursue normal operations until any possible sale is final.

### **TSBC/Aegon Retention Efforts**

- Transamerica has provided an effective retention program to maintain our experienced servicing and liquidation staff during the sale process.
  - All employees who are not offered a comparable position by the purchaser will receive six months severance with a minimum sixty-day notice.
  - This is Transamerica's standard retention benefit during the sale. Additional incentives apply to 40% of the employees, who had been designated “key employees” in January, 2001.
  - Up to now, this retention program has successfully minimized turnover during the sale process.
  - However, as the sale process progresses, these retention measures have begun to lose their effectiveness. Employees both with and without additional incentives have begun to entertain other job offers, making employee retention a potential operational risk.

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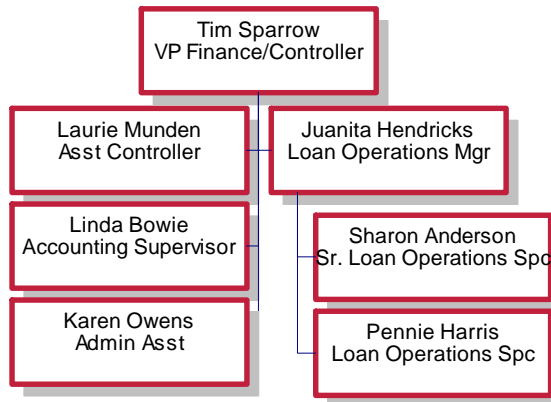
## Finance and Loan Operations

### *Tim Sparrow*

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### People

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Unlike a typical bank setup the loan operations area in TSBC reports to the head of Finance because of the close working relationship necessary between accounting and loan operations. This relationship is necessary to meet all of the investor reporting responsibilities of the business activities.

### Functions

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- Finance fulfills the needs for loan operations and accounting.
  - Accounting at the business unit level is necessary due to the intricate issues created by the participation accounting, securitization transactions and the separate audit requirement.
  - Loan operations facilitates the daily maintenance of the loan system in every respect (payment posting, for example).

### Accomplishments

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- Improved remittance accounting processes, procedures and documentation
- More timely preparation and remittance of SBA 172 payments
- Successfully shifted the workload to fewer people, while maintaining healthy working atmosphere
- Improved processes and procedures related to responses to Colson inquiries
- Enhanced communication between the liquidation/servicing groups and finance
- Achieved the highest possible rating on SBLC examination even with the examiners for the first time audited detailed financial procedures and reporting

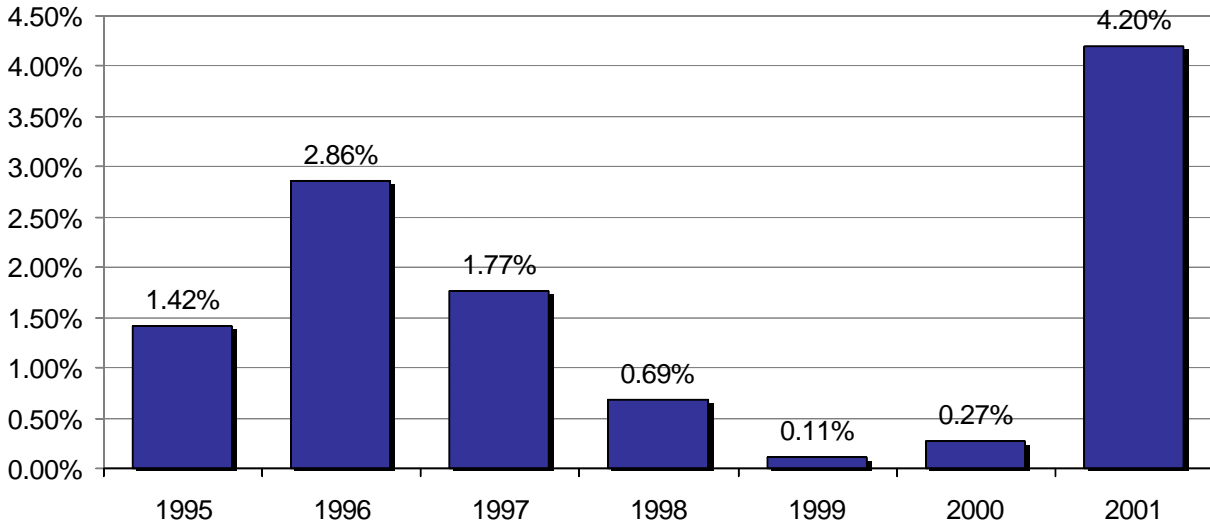
### Risks

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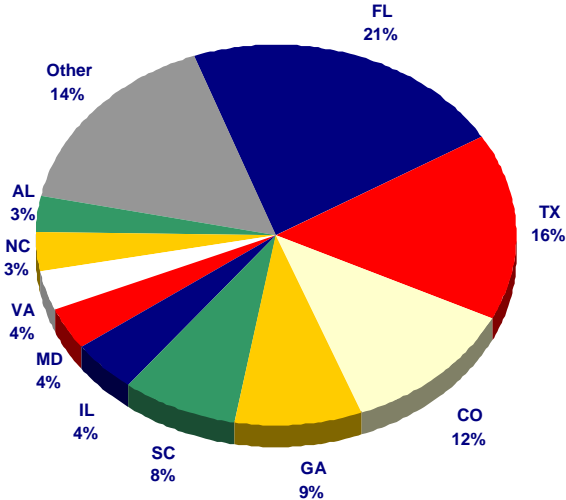
- Failure to maintain the loan system properly will adversely affect our borrowers and internal departments and our fiduciary obligations to our investors.
- Lack of adequate internal controls and timely, accurate reporting could expose the company to financial loss or being out of compliance with federal regulations.
- The primary balance sheet risk is the *valuation* of assets and liabilities, most notably, loans receivable (allowance), real estate owned, SBA receivables and residual assets (I/O strip, investment in NABS).

# Finance at a glance

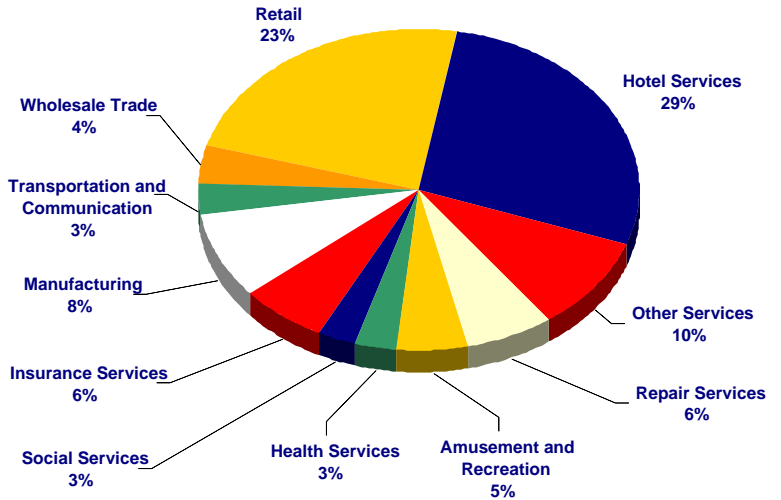
## Net Charge-offs by Year



## Loan Portfolio by Geography



## Loan Portfolio by Industry



- Securitization of the unguaranteed loan amount:
  - 1995: \$17.1 million
  - 1996: \$17.5 million
  - 1997: \$21.5 million
- Approximately \$18.2 million of securitized unguaranteed loans remain outstanding as of 8/31/01

## Details

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### **Major differences in accounting and loan operations from conventional loan portfolios:**

1. Each loan has a guaranteed and unguaranteed portion
  - Requires splitting of liquidation expenses
  - Recoveries/charge-offs can require several different accounting presentations
  - Allowance calculations are effected
  - REO presentation is effected
2. Multiple sold participations
3. Accounting for repurchased loans accounting (for loans repurchased by the SBA)
4. Investor reporting
  - 1502, both daily and monthly (gtd. loans sold)
  - Remittance accounting
  - SBA Form 172 (for loans repurchased by SBA)
  - Complications for most types of servicing actions and liquidation actions
5. Securitization accounting and reporting
  - The securitization pools are comprised of only the unguaranteed portion of the loans, making everything involving loans in the pools more difficult to handle.
  - Daily wires to restricted cash accounts
  - Remittance accounting
  - Multiple participation strips on each loan
  - Monthly servicer's certificates
  - Residual assets
  - Restricted cash accounts
6. Assets held for sale accounting for TA reporting purposes

### **Accomplishments in Detail:**

- Improved remittance accounting processes/procedures/documentation
- More timely preparation and remittance of SBA 172 payments
- 3 audits/examinations and due diligence throughout 2001
- SBLC examiners, for the first time, focused on review of 1502 reporting process (reconciliation and timely resolution of discrepancies) and found no weaknesses in TSBC procedures.
- Electronic filing of 1098's
- Automation of daily loan system entries to ledger
- Documentation of all major procedures and processes
- Shut down of outlying offices
- Clean up and on-going monitoring of SBA receivable
- Many, many ad hoc reporting projects throughout the year

## Specific functions of employees:

### Loan Operations Staff, Pennie & Sharon

#### Daily:

- Post payments
- Balance payment and disbursement activity to cash
- Generate SBA Form 172 for payments received on loans repurchased by SBA
- 1502 remittances for late payments and payoffs
- Generate system reports
- Provide payoff quotes to borrowers
- Handle incoming payments not send to the company lockbox- requires daily deposit
- Initiate wires to restricted cash accounts for payments received on securitized loans
- Routine file maintenance
- Resolve Colson discrepancies
- Prepare certain accounting schedules, such as advances summary and prepare journal entries for loan system activity

#### Monthly:

- Generate and mail billing statements
- File maintenance for repurchases/REO transactions/charge-offs/non-earning changes, etc
- Monthly 1502
- Assess late fees (twice per month)
- Handle advanced customer service issues
- Process participation transactions

### Loan Operations Manager, Juanita

- Supervise Pennie & Sharon
- Quarterly rate changes
- Yearly 1098 reporting to IRS and borrowers
- Final authority on customer service issues requiring a technical understanding of the loan system and the amortization process
- Review and approve all 172 payments and 1502 remittances
- Resolve SBA and Colson issues

### Administrative Assistant, Karen Owens

- Fulfills most functions of an office manager; handles all the day to day needs of the entire office.
- Processes all A/P items (IPF's) going to Chicago, and generates IPF's for bills coming directly to accounting
- Functions as backup receptionist
- Performs many miscellaneous duties for the entire executive staff

### V. P. of Finance, Tim Sparrow

- Supervise all accounting and loan operations staff
- Review and sign monthly servicer's certificates
- Monitor capital requirement
- Monitor residual assets valuations
- Review all schedules sent to Corp for reporting
- Monitor account balances for accuracy
- Generate various reports during the month and at month end

### Accounting Supervisor, Linda Bowie

- Reconciles cash activity on a daily basis
- Generates journal entries as needed
- Performs all actions necessary to follow and reconcile the remittance accounting
- Reconciles the loan system activity to cash on a daily basis
- Generates month end schedules
- Performs all bank reconciliations
- Monitors ledgers and accounts for any unusual activity

### Assistant Controller, Laurie Munden

- Review and approve all A/P prior to sending it to Chicago
- Review and approve all wires prior to sending the to Treasury
- Initiate monthly ACH for customer payments
- Prepare monthly servicer's certificates
- Performs the monthly close of the loan system
- Prepares monthly schedules and management book
- Spreads financial statement for servicing group
- Review and approve all journal entries
- Many ad hoc special projects as needed

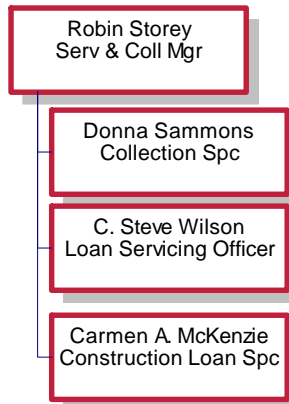
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## Collection and Servicing

### *Robin Storey*

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### People



In August of 2001, the servicing department lost Bill Baxley, an experienced SBA servicing officer. Ward Hickey has stepped in to help with the servicing load and Laurie Munden has helped by spreading borrower financial statements. In addition, we are working on additional adjustments to the work flow to utilize members of the loan documentation team for some servicing-related tasks. However, staffing in the servicing area remains a critical issue and stands to jeopardize the gains we have made in servicing quality over the last 10 months.

### Functions

- Collection of past due payments
- Force Place Insurance
- Service existing portfolio, including loan assumptions, deferments, collateral substitutions and releases, risk rating adjustments and some workout efforts
- Processing of servicing and liquidation expenses for borrower accounts
- Disbursements for remaining construction loans

### Accomplishments

- Established weekly staff meetings to discuss past due accounts and review risk ratings.
- Developed database for Servicing Requests and computerized Servicing Request form. Still in design stage is the Status Change Form.
- Divided territory and assigned Servicing Officer to service the assigned territory.
- Standardized financial reviews of borrowers.
- Began timely review of risk ratings.
- Asked internal legal counsel to review collection letters.
- Most recent PLP exam found no material weaknesses in technical compliance.
- Recent SBLC exam recognized improvements in credit administration and risk identification, i.e., more dynamic risk rating (proper risk identification), review of financial statements.

### Risks

- Staffing problems threaten the quality and timeliness of servicing efforts.
- Improper documentation of servicing actions can jeopardize the SBA guarantee.

## Details

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### Collection Tasks

- Call borrower's to obtain past due payments, determine why past due and request financial statements
- Send default letters when over 30 days past due
- Send various other collection letters when appropriate
- Force place insurance when necessary
- Answer billing questions from borrowers

### Servicing Tasks

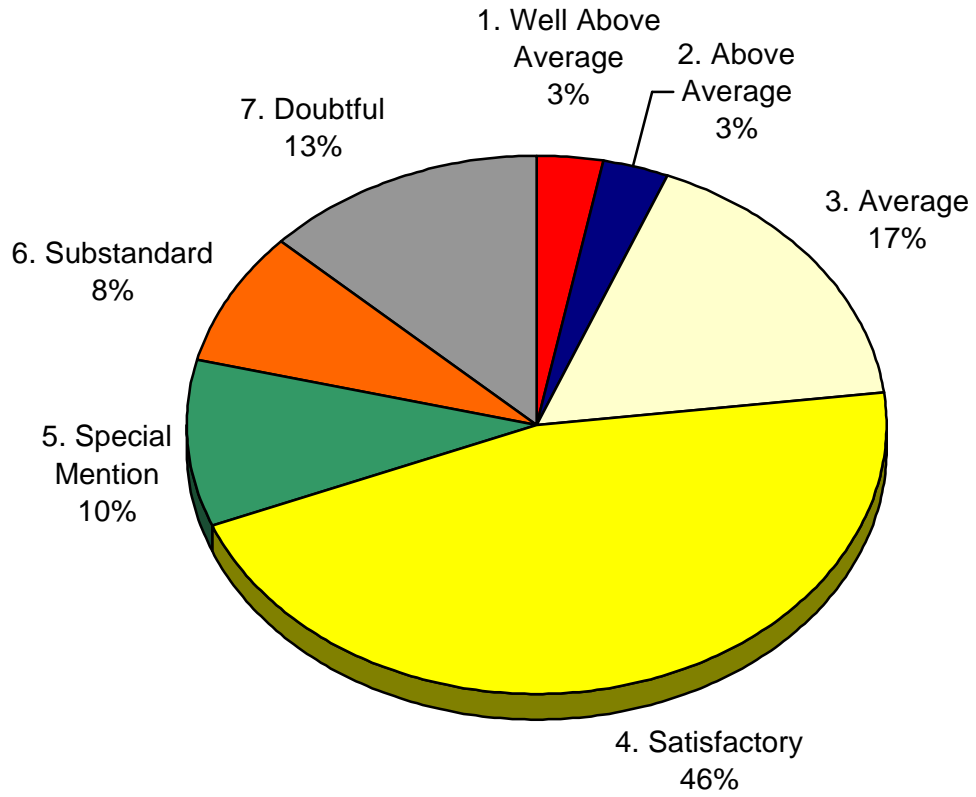
- Assist in difficult collection situations
- Handle servicing actions, i.e., Deferments, assumptions, collateral release/substitution, subordination, rate reductions, etc.
- Knowledge of SOP 5010 (Loan processing) is necessary for servicing actions in addition to SOP 5050 (Loan Servicing)
- The Loan Authorization must be updated on servicing actions (327 Action Report)
- Analyze financial statements from borrowers and ascertain appropriate risk rating
- Maintain rapport with SBA Servicing Offices (Little Rock and Fresno) as well as Districts
- All loans are serviced under the PLP authority per the 750 agreement
- Some servicing actions require prior SBA approval or notification (See handout)
- Must notify or obtain approval from Colson (Investors) on deferral of payments
- Monitor warranty reserve risk
- Improper handling of servicing actions can result in guarantee repairs
- Construction Draws

## Risk Rating System

TSBC's numeric grading system is a comprehensive compilation of five credit factors including Management, Repayment Ability, Collateral, Credit and Equity. The narrative supporting the grading system is similar to that used in the National Banking System. Regional Credit Managers initially established the grade of a new credit, subject to review by Portfolio Management. The Servicing and Liquidation Departments review and adjust the loan grades periodically in conjunction with receipt of annual financial statements, or immediately, upon any change in the overall status of a credit.

GRADE	DESCRIPTION
1	<u>WELL ABOVE AVERAGE</u> : Primary and secondary sources of repayment are excellent. Business is well established and stable, and exhibits positive trends. Historical cash flow levels, as reflected in financial statements or demonstrated in routine seasonal asset contraction, provide an assured and comfortable source of repayment. Financial condition reflects minimum leverage and sufficient liquidity to meet all obligations as they come due. Guarantees provide sufficient outside strength so as to provide an acceptable tertiary source of repayment.
2	<u>ABOVE AVERAGE</u> : Primary source of repayment is good and the secondary source is adequate. Business is well established and principals have had successful experience in the field. Historical cash flow levels, or demonstrated routine seasonal asset contraction, provide a source of repayment, which includes a protective margin. The financial condition is not more than moderately leveraged and is adequately liquid to meet obligations. Guarantees are strong enough to provide additional cash flow or repayment enhancement to the credit.
3	<u>AVERAGE</u> : The primary source of repayment is satisfactory and the secondary source is fair. Collateral values should cover the loan in the event of a forced liquidation. While the business may be somewhat new, the principals have had adequate experience in this industry or management experience in another industry. Cash flow or normal seasonal asset contraction is expected to be sufficient to meet scheduled repayment of the loan, even though historical earnings may have been marginal and/or volatile. Capital and liquidity are slightly below average. Guarantees could, if necessary, cover a loan shortfall if the business failed.
4	<u>SATISFACTORY</u> : The primary source of repayment is fair and may be based on projections. Collateral assets that secure the loan may be insufficient to cover the loan in the event of a forced liquidation. The business may be new and/or the principals may have little or no direct experience in the field. Cash flow is projected to be adequate to meet the scheduled-repayment of the loan, even though historical earnings may have been deficient or nonexistent. Capital and liquidity may be below average, and the guarantors may have limited financial strength to sustain the credit through a downturn or business failure.
5	<u>SPECIAL MENTION</u> : Currently protected but some potential weakness may exist that constitutes a higher than average credit risk. Primary source of repayment may be based strictly on projections. Collateral may be insufficient to cover the amount of the loan in the event of a forced liquidation. Management may be new to the industry and have no direct experience. Capital and liquidity are below average, and the guarantors add limited financial strength to the credit. If performance is not documented within six months, the credit may be downgraded to Substandard.
6	<u>SUBSTANDARD</u> : Substantial and unreasonable credit risk to the company by reason of an unfavorable payment record, unfavorable statement ratios, negative trends, insufficient credit and/or financial data, and lack of proper documentation which requires the continual attention of Portfolio Management. A plan must be developed for reducing exposure as rapidly as possible under the presumption that the credit cannot be financed elsewhere. Portfolio Management must approve any extensions, deferrals or forbearance.
7	<u>DOUBTFUL</u> : Chance of loss is high and there is a high reliance on collateral liquidation for repayment. Credit is deemed uncollectible, except for the collateral liquidation. Continuation with the credit without proceeding against collateral is unacceptable unless the exposure is being controlled in bankruptcy proceedings. Identified deficiencies will be charged off within the current operating quarter.

### Loan Portfolio by Risk Classification



## **Summary of PLP Servicing Actions**

Lenders may service loans approved under PLP procedures using generally accepted commercial banking standards employed by prudent lenders. However, there are certain things regarding SBA loans that the lender may never do, may do only with SBA approval, or may do with notice to SBA.

### ***NEVER:***

- Take any action that confers a preference on the lender

### ***ACTIONS REQUIRING SBA APPROVAL:***

- Compromise on the principal balance
- Release Guarantor/Maker if loan is not current or liquidation anticipated
- Title property in the name of SBA
- Take title to property that is environmentally impaired
- Transfer a loan to another lender
- Sell or pledge more than 90% of a loan
- Increase in loan amount
- Change in guaranty %
- Repurchase from secondary market
- Handle any litigation involving legal costs exceeding \$5,000

### ***MUST NOTIFY SBA:***

- Decrease the principal amount of the loan
- Cancel the loan
- Change the trade name of the business
- Change the borrower's address
- Change the interest rate on a fixed rate loan or the interest rate spread on a variable rate loan
- Change the loan's maturity
- Handle a situation that requires SBA to re-classify into "liquidation status"

(In other words, any action that would cause a change in SBA's database or change the note terms)

**Differences in SBA Lender Authority**

<i>Action</i>	<i>General Program</i>	<i>Certified Lender Program</i>	<i>Preferred Lenders Program</i>
Liquidation Plan	LQ Plan + underwriting characteristics must be sent to SBA for approval in advance of liquidating collateral	LQ Plan + underwriting characteristics must be sent to SBA for approval in advance of liquidation. SBA must respond within 10 business days or it is approved. If the principal balance is \$50,000 or less, the LQ plan is not required to be submitted. If the principal balance is \$50,000 or less, to SBA until guaranty purchase	LQ Plan + underwriting characteristics are required prior to recovery actions. Lenders send a copy of the plan at the time of their request for guaranty purchase on loans with principal balances more than \$50,000 On all loans, the LQ plan + changes must be submitted with the final Wrap Up Report at completion of the recovery process.
Site Visits	Lender must make a site visit and document within 60 days of unremedied default in payment or as soon as possible after default if there are assets of significant value then could be removed or depleted. A site visit must be conducted within 15 days of a liquidation event Site visit reports will be reviewed at time of guaranty purchase	SAME as General Program	SAME as General Program. If the site visit is waived under appropriate circumstances the waiver must be documented by the lender in the loan file.
Guaranty Purchase	SBA will purchase the gtd portion after 60 days past due. SBA may agree to purchase the gty if the loan is less than 60 days past due when the loan is classified "in liquidation"	SAME as General Program	SBA will purchase the gtd portion after 60 days past due SBA "encourages" the lender to liquidate worthwhile collateral prior gty purchase (not required) SBA may agree to gty purchase if the loan is less than 60 days past due when the loan is classified "in liquidation" status
Progress Reports	The lender must submit quarterly status updates for 1) all cases beginning at the time of guaranty purchase and 2) acquire real property (COLPUR) beginning 6 months after acquisition	SAME as General Program	SAME as General Program
Protective Bids	SBA must approve the lender's protective bid and to subsequent changes of more than 10% if a protective bid is entered	SAME as General Program	No prior SBA approval required
Wrap Up Reports	None	None	The lender must provide a Wrap Up Report when it is determined that the loan will not be fully repaid after all worthwhile collateral has been liquidated and no further recoveries are anticipated The lender must provide a Wrap Up Report if liquidation is complete and guaranty purchase is requested.
Expenses	Expenses must be approved through the liquidation plan legal fees must not exceed more than 10% of the amount agreed	SAME as General Program	SBA will share in reasonable and necessary expenses on a pro-rata basis up to SBA's share of total recoveries. Lender must get SBA approval for fees exceeding \$5,000.

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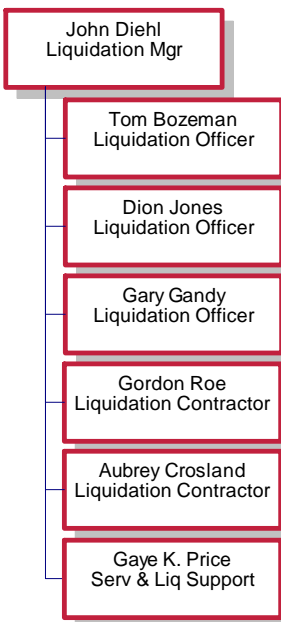
# Liquidation

## John Diehl

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### People

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Experience and expertise mark the liquidation staff at TSBC. Two liquidators are former SBA employees, one is an attorney and all understand the rigors of SBA liquidation. Ten months ago, the liquidation staff was smaller and the account load for each liquidator was inefficient. Through internal restructuring, TSBC brought more resources to bear on liquidation and, in May of 2001, hired two contract liquidators to further improve the strength of the department.

### Functions

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- Preserve the SBA guaranty on individual loans
- Identify potential loan losses, reduce problem loan and loss exposure
- Maximize loan recovery and minimize losses
- Manage all non-performing accounts, generally 90+ days past due
- SBA guaranty settlement

### Accomplishments

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- Increased staffing levels and reduced account loads.
- Created new admin position to assist liquidation department.
- Separated liquidation and servicing functions to better utilize staff.
- SBLC exam noted improvements over liquidation evaluations in previous years.

### Risks

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- Failure to follow SBA procedures resulting in partial or full denial of SBA guarantee including out-of-pocket costs normally pro-rated between SBA and lender.
- Poorly collateralized loans, especially those originated in 1999-2000, present significant loss risk.
- Shifting SBA priorities, procedural changes and differences among SBA offices make standardizing procedures difficult.
- Administrative costs will significantly increase if PLP servicing and liquidation authority is not maintained.
- Even though loads have improved, staff fatigue and morale are still affected by heavy workload and increasing SBA guaranty issues.

## Details

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### Liquidation Accounts Trend for 7(a) and 504 loans

<i>Date</i>	<i>Number of Accounts</i>	<i>Total GL Balance</i>
12/31/99	41	\$15,267,000
12/31/00	66	\$30,350,000
7/31/01	109	\$42,813,000

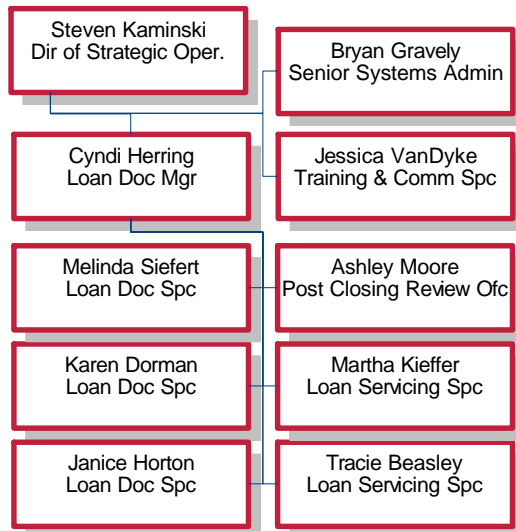
### Liquidation Basics

- Primary contact for borrower, guarantors
  - Develop and implement workout or liquidation strategy – acceleration, debt restructure, foreclosure, bankruptcy, collateral/REO disposition, deficiency collection from guarantors
  - Hire and supervise outside professionals to assist TSBC, e.g. attorney, appraiser, auctioneer, environmental engineer, real estate broker
  - Internal reporting, e.g. classified asset schedule, impaired asset reports
- Compliance with SBA SOP liquidation activities
  - Primary contact for respective SBA district office
  - Notification, reporting requirements
  - Solicit SBA concurrence for key liquidation activities (PLP v. non-PLP status)
    - PLP authority limitations
- SBA guaranty settlement, including final wrap up
  - SBA guaranty repair issues
- SBA Inspector General investigations
- Direct contact for SBA compliance and safety and soundness audits

# General Operations

## Steve Kaminski

### People



The production shutdown left TSBC a backlog of document exceptions on loans that had already closed. To address this problem, TSBC assembled a team of documentation specialists, some of whom came from loan production, to clear these exceptions and prepare for upcoming audits. This team falls under the heading of general operations along with IT.

### Functions

- To audit files in the portfolio to identify any documentation exceptions and to clear those exceptions, if possible.
- To maintain the loan files, including updating UCC & insurance renewals.
- To document any approved servicing actions
- To provide IT support for TSBC and to define, automate and improve processes overall

### Accomplishments

- Defined stricter file-handling procedures
- Defined procedures for UCC filings and insurance renewals
- Helped automate servicing request and document exception tracking
- Provided documentation and file support for sale due diligence
- Supported servicing and liquidation documentation requests
- Contributed to successful government audits by appropriate document control

### Risks

- Some outstanding documentation exceptions could result in an SBA guarantee repair.
- Failure to properly document a servicing or liquidation action could result in loan loss.
- Persistent lapses in loan documentation could result in loss of PLP servicing authority.
- Improper loan documentation can complicate interaction with SBA and other third parties.

## Details

### Guarantee Exposure by Exception Type

The loans with the identified exceptions are performing; however, the exceptions noted could result in a guaranty repair for the exposure amount given if the loan were to go into liquidation.

<i>Exception Type</i>	<i>Exposure</i>	<i>Number of Loans</i>
Dismissals of Liens-Tax Judgments	\$506	1
Equity Injection back-up documentation	\$318,000	5
Recorded Assignment of Life Insurance Policy	\$3,645,197	13
Recorded Mortgage(s) or Deed(s) of Trust	\$1,053,000	3
Recorded UCC's - County	\$219,238	2
Standby-Subordination Agreement	\$40,000	1
<i>Total</i>	<i>\$5,275,941</i>	<i>25</i>

### TSBC Bi-weekly staffing levels since November, 2000

<i>Date</i>	<i>Census</i>	<i>Number Lost</i>	<i>TARRPed</i>	<i>Resigned</i>
11/15/2000	90	0		
11/30/2000	46	-44	First Wave	
12/15/2000	43	-3	Don Ford, Steve Wilson, Julie Bullock	
12/30/2000	42	-1	Trish Reaves	
1/15/2001	42	0		
1/30/2001	41	-1		Delores Kennon
2/15/2001	40	-1	Craig Kaffenberger	
2/28/2001	35	-5	Ruth Ann Lewis, Tanya Park, Paul Burch, Jeff Moyer	Nancy Revis
3/15/2001	35	0		
3/30/2001	35	0		
4/15/2001	35	0		
4/30/2001	35	0		
5/15/2001	35	0		
5/30/2001	33	-2	Jill Harbin, Marlene Pindroh	
6/15/2001	33	0		
6/30/2001	33	0		
7/15/2001	32	-1	Bonnie Waites	
7/30/2001	32	0		
8/15/2001	31	-1		Bill Baxley (deceased)
8/30/2001	29	-2		Chris Alexander, Kathy Barnette
9/15/2001	29	0		
9/30/2001	29	0		

## Loan Documentation and General Operational Staff

### **Cyndi Herring, Loan Documentation Manager**

- Manage and Train Loan Documentation Team
- Coordinate servicing and liquidation documentation requests
- Sell the Guaranteed portion of SBA 7(a) loans
- Certify project costs and fund CDC Debenture on 504 loans
- Oversee Colson, Carolina First Bank, and First Union as Trustee(s) for TSBC's Notes, Mortgages, etc.
- Review loans for application, closing, and documentation errors and obtain any cited or pending items

### **Martha Kieffer & Tracie Beasley, Loan Servicing Specialists**

- Maintain Property, Flood, Liability, and Life Insurance Database
- File documentation in application, credit, and vault files
- Process releases and documentation for paid out loans
- Assist Servicing and Liquidation personnel in matters pertaining to files

### **Karen Dorman, Loan Documentation Specialist**

- Maintain UCC Database and file UCC Continuations as necessary
- Review loans for application, closing, construction, and documentation errors and obtain any cited or pending items
- Prepare necessary paperwork to document servicing requests

### **Janice Horton, Loan Documentation Specialist**

- Review loans for application, closing, legal, and documentation errors and obtain any cited or pending items
- Prepare necessary paperwork to document servicing requests

### **Ashley Moore, Post-Closing Review Officer**

- Review loans for application, closing, and documentation errors and obtain any cited or pending items
- Prepare necessary paperwork to document servicing requests

### **Melinda Siefert, Loan Documentation Specialist**

- Obtain any missing or pending items as cited in Audits
- Prepare necessary paperwork to document servicing Requests

### **Jessica VanDyke, Training and Communication Specialist**

- Provide business process analysis for automation projects
- Develop software systems for process automation
- Coordinate business process development
- Provide PC software support
- Assist servicing & loan documentation
- Coordinate various training events across the company, e.g. new hire training, special functional training, etc.
- Assist in internal marketing and communication efforts
- Conduct technology training as needed.
- Assist special projects & events

### **Steve Kaminski, Director of Strategic Operations**

- Direct execution of business plans and special projects
- Direct process definition and automation
- Direct internal communication
- Direct company-wide resource planning & recruit new personnel
- Supervise loan documentation
- Assist in government relations
- Direct internal marketing efforts
- Supervise general operations including facilities, equipment and technology
- Supervise user training
- Plan, supervise and, if necessary, execute software development projects
- Develop and monitor training programs

### **Bryan Gravely, Senior System Administrator**

- Maintain Lotus Notes E-mail & Servers, General Network Operations
- Maintain System Security
- Maintain software licensing
- Maintain facility security and coordinates maintenance
- Maintain telephone system
- Execute special IT projects
- Support Internet Access and Projects
- Maintain PC Hardware
- Maintain PC Software
- Maintain Novell Netware Servers and network, Microsoft NT Servers and network, Local Area Network
- Maintain Loan Accounting system (PCFS)
- Maintain Lotus Notes Databases

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## Government Relations

*Ward Hickey*

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### People

Ward Hickey  
Director, Govt Relations

Even after the production shutdown, government relations was a priority at TSBC. We have had two successful government audits and must renew our PLP status in November, 2001.

### Functions

- Maintain a close relationship with the SBA national office as a strategic partnership throughout 40 PLP state district offices & 8 regions.
- Maintain PLP delegated authority to originate, service & liquidate loans.
- Insure a pro-active “Best Practices” Risk Management perspective with Office of Financial Assistance/Lender Oversight & SBA field examining units, including:
  - Farm Credit Administration (FCA) in VA for Safety & Soundness.
  - SBA PLP Audit team in KC MO for Portfolio Technical Compliance Reviews.

### Accomplishments

- Two successive PLP Compliance exams (2000-2001) earning the highest SBA designation, “Substantially In Compliance”
- Two successive Safety & Soundness exams (2000-2001) earning satisfactory rating, a passing grade indicating no instances of material adverse weaknesses.

### Risks

- Failure to maintain a strategic & tactical partnership with the SBA may result in Non-PLP status, causing a loss of “unilateral PLP lending authority”
- A loss of PLP authority would force TSBC to receive prior approval for all servicing and liquidation actions from the specific SBA district office involved in the account.

### Details

- TSBC, as successor to EBC, qualified as an expert lender in the SBA Preferred Lenders Program (PLP). TSBC legally operates as a lender with a 750 loan agreement (subject to termination by either SBA/TSBC with 10 days notice) while its PLP 1347 agreement expires 11/30/01.
- Contact to renew PLP status has been made with the National PLP Center in Sacramento.
- PLP participants have delegated lending authority to approve and fund loans without prior SBA approval & accordingly are delegated “unilateral authority” to service & liquidate their SBA loan portfolios.
- SBA lender oversight is conducted via on-site yearly examinations.



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## **Agenda-SBA Oversight/Transition/HR Issues**

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### **SBA Oversight/ “Residual” Issues**

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- 1) Examinations
  - a. Preferred Lender Program
  - b. Safety and Soundness
  - c. Audit Requirement
- 2) Conditions for Sub-Servicing Arrangements
- 3) PLP Servicing/Liquidation Status
  - a) SBA relationship is one of partnership
  - b) Significant difficulties if not PLP servicer

### **Transition Issues**

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- TA involvement after the sale and transfer of servicing
- TA has guaranty risk for all loans not sold
- TA may have guaranty risk for loans sold
- Purchaser retention issues during transition

### **HR Issues**

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- 60-Day Notice Issue
- Morale
- Status of sale
- Proposed Transaction—how does this affect me?
- Retention is becoming a major concern