The Arizona Banker

PUB. 10 2020 ISSUE 3

Resources for Black Business Owners and Entrepreneurs

Official Publication of the Arizona Bankers Association

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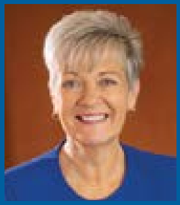

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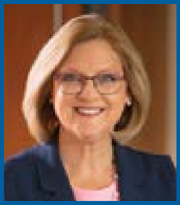

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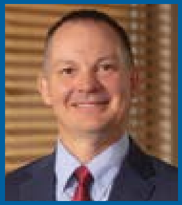

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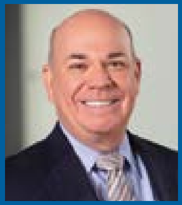

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CHAIRMAN'S VIEW

By Laurie Stewart

Rising to the Challenge

AFTER MONTHS OF GROWING ALL-TOO-FAMILIAR WITH THE INTERIOR of my home — and the aisles of the local grocery store where toilet paper, hand sanitizer and all-purpose flour are stored, or not — it's hard to think back on what I had planned to be doing before COVID-19 became a reality and rapidly changed how our nation lived and worked. In that pre-virus world, I anticipated traveling around the country talking with bankers from Mississippi to Wisconsin about the challenges they were facing at their banks — and what the American Bankers Association could do to help.

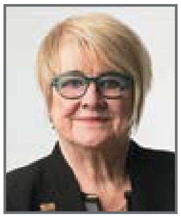
As someone who thrives on peer interaction, I've missed speaking with so many of you in person. But thanks to the efforts of the ABA staff — working hand-in-hand with the state bankers associations — I have benefited from the wealth of resources available to help my bank navigate through this crisis. With a steady stream of breaking news shared through Daily Newsbytes, CEO Updates, ABA Banking Journal stories and a host of podcasts, webinars and other critical resources, we have been able to keep abreast of the biggest developments affecting our customers — while watching with pride at how bankers have risen to the challenge of this pandemic, with its record unemployment and financial pain.

In the process, our industry has shown what it is made of — dedicated employees working around-the-clock to help customers shore up their financial lives. Stationed at kitchen tables, in spare bedrooms, laundry rooms and makeshift basement offices, bankers transformed themselves into an informed and dedicated army of workers in order to assist customers under extraordinary circumstances. From working through the early glitches in the Paycheck Protection Program — so that thousands of small business owners could secure the loans they needed to stay afloat — to helping millions of customers who had lost their jobs find temporary relief through mortgage forbearance and debt restructuring programs.

As I told Marketplace host Kai Ryssdal during an interview, my bank in Seattle received five times the number of PPP applications for loan assistance than we originally anticipated. During that initial lending phase, we had no idea how many small businesses were starving for funds. So, like many bankers across the country, our staff worked day and night to process the loans as quickly as possible, before funds ran out. By the end of the first phase of the program, we had completed the same number of loans in two weeks that we normally handle in six months. It's a feat that would have been impossible without the willingness of the staff to step up to the challenge, even when it meant working late on a Saturday evening and getting up on Sunday to start all over again.

I couldn't be prouder of the role my employees — and bankers all across the country — have played in supporting their communities and keeping the economy running. As the beloved children's television host Fred Rogers once said: "Real strength has to do with helping others." In this regard, our industry has shown what it is made of. Whether waiving transaction and processing fees, offering payment extensions, providing emergency lines of credit, donating computers to local schools or using bank kitchens to prepare food for homeless shelters, we can all be proud of the important role we've played during this daunting time.

Perhaps NPR's Weekend Edition host Scott Simon said it best in an essay marking his daughter's 17th birthday. He wondered aloud at what his girls would remember when they looked back at this time. "I hope," he said, "they'll remember how many good people worked so hard to keep the world running."



ABA Chair Laurie Stewart is president and CEO of Sound Community Bank, Seattle. This article originally appeared in the ABA Banking Journal and is republished here with permission.

The AzBA's First Virtual Annual Meeting

Resources for Black Business Owners and Entrepreneurs

STARTING YOUR OWN BUSINESS is a challenging but exciting and rewarding achievement. Entrepreneurs face a variety of obstacles when starting a new venture, from obtaining financing, hiring a team, marketing their product or service, keeping up with competitors, and so much more. For some Black entrepreneurs and business owners, these challenges can be even harder to overcome.

A study by Guidant Financial found out of all the challenges Black entrepreneurs face, one of the most prevalent is lack of funding. For most entrepreneurs, regardless of race, obtaining financing is often the most significant challenge to getting their business up and running. Many entrepreneurs first look to family and other social connections to raise funding. For many Black entrepreneurs, the racial wealth gap means we almost inevitably start with less capital.

It's worth the effort to overcome these challenges for those who want to become their own boss and pursue their passion. The good news is, there are a variety of resources specifically set up to help Black entrepreneurs and business owners push beyond obstacles and achieve their dreams and goals. Take a look at some of these local and national resources.

Black Chamber of Arizona

The Black Chamber of Arizona connects Black entrepreneurs and business owners in Arizona by facilitating relationships between Chamber members and between Black-owned businesses, and the greater Phoenix corporate community. The Black Chamber of Arizona also provides education and training to its members, and they are an active political advocate for policies that address Black business's challenges.

Minority Business Development Agency (MBDA)

MBDA is an agency of the U.S. Department of Commerce that promotes minority-owned

Funding is an essential factor in getting your business up and running, and maintaining capital is vital in ensuring your business continues to succeed, but often overlooked is the importance of networking with members outside the community to expand our reach.

business growth by linking minority-owned businesses with the capital, contracts and markets they need to grow.

They also serve as subject matter experts and advocates for the minority business community by providing free educational content and loan and grant opportunities, including a loan opportunity specifically for Black women business owners.

National Minority Supplier Development Council (NMSDC)

NMSDC's mission is to connect minority-owned organizations, big and small, with a vast network of corporate members who wish to buy products, services and solutions from minority-owned businesses. Corporate membership includes the largest public and privately owned companies, and health care companies, colleges and universities. NMSDC also helps businesses complete the minority business enterprise (MBE) certification process often needed to obtain other minority-owned business benefits.

U.S. Small Business Administration (SBA)

While the SBA services all U.S. small businesses, its 8(a) Business Development program specifically sets out to assist minority-owned businesses, including Black-owned businesses, by providing revenue generation opportunities through government contracting. To qualify for the program, you must first certify your business is an 8(a) business, which you can do on the SBA website.

Look Beyond Funding

One commonality among the Black entrepreneurs and business owners I've seen succeed is an unwavering focus on marketing their business and networking with everyone who is an ally. Funding is an essential factor in getting your business up and running, and maintaining capital is vital in ensuring your business continues to succeed, but often overlooked is the importance of networking with members outside the community to expand our reach.

Our community is a good place to establish connections and resources through all stages; however, continue connecting with those outside the Black community and expand relationships outside your typical market. Remember, a resource may not always be funding. A resource can be a mentor or an advocate willing to promote your product, service or brand.

The Bottom Line

All entrepreneurs share a lifelong dream of starting and growing a business. Unfortunately, Black entrepreneurs and business

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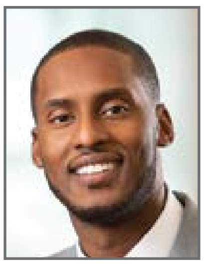
owners still face an unfair struggle in some areas. Thankfully, federal and local programs are available to provide educational tools, funding resources and network-building opportunities.

According to the U.S. Census Bureau's latest figures, the number of Black-owned businesses is on the rise. As long as we are provided support and opportunities, our businesses will flourish, and in turn, our communities will thrive.

When you're ready to take the leap toward owning your own business, or you're ready to grow your existing business, know you have educational tools, funding resources and network building opportunities to help achieve your dream.



D'Angelo Johnson is vice president, private banking manager at Bankers Trust. He has 16 years of banking and financial services experience. He can be reached at DJohnson@BankersTrust.com

ARIZONA BANKERS ASSOCIATION

Jack Barry, Chairman & CEO at Enterprise Bank

Thank You!
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Jack Barry

The Association is grateful for your hard work and your tireless commitment to the industry and leadership in Arizona

CFPB Announces Its Spring Agenda

By Chris Bell, Associate General Cousel, Compliance Alliance

THE CHALLENGES WE HAVE FACED in 2020 have come at us out of nowhere and at a lightning pace. The world continues to face a global pandemic, while regulators and businesses are largely reinventing significant industries. We have dealt with the Paycheck Protection Program, stimulus checks, mountains of loan modification requests, significant pushes to online services, and many other things that were not on our 2020 roadmap. With so many unexpected developments, it's nice when we have the opportunity to anticipate some of the changes that will require us to take action.

The Consumer Finance Protection Bureau (CFPB) has been busy during the last several months, and the next 12 months promise even more change. The CFPB recently published its spring 2020 Agenda as part of the Trump administration's spring 2020 Unified Agenda of Federal Regulatory and Deregulatory Actions. The agency recapped some of its actions from recent months and gave us a preview of the regulatory roadmap through spring 2021. Many of the changes follow up on proposals the agency had already announced.

Changes are underway to the escrow requirements of higher-priced mortgage loans (HPMLs). Under Section 108 of the Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018 (EGRRCPA), Congress instructed the CFPB to conduct a rulemaking to exempt loans from the HPLM escrow requirements if the lender has $10 billion or less in assets and meets other criteria. The CFPB published a notice of proposed rulemaking on July 2 to implement Section 108 of the EGRRCPA. Comments are due by Sept. 21, 2020.

As we enter fall, the CFPB plans to take a significant step toward implementing section 1071 of the Dodd-Frank Act. Section 1071 requires lenders to identify women-owned, minority-owned, and small businesses, and to collect data related to race, sex, and ethnicity of the business owners, the purpose of the loan, the action taken regarding the loan, the business's gross annual revenue, and "any additional data that the [CFPB] determines would aid in fulfilling the purposes of this section." In October, the CFPB will convene a panel under the Small Business Regulatory Enforcement Fairness Act to discuss this matter. Ahead of the event, the CFPB will be releasing materials that the group will discuss with representatives of small entities likely to be directly affected by the bureau's rule to implement section 1071.

The fall will also likely see two proposals to modify the Home Mortgage Disclosure Act (HMDA). The first proposal follows the May 2019 advance notice of proposed rulemaking concerning data points that banks must report under the 2015 HMDA rule and coverage of business or commercial purpose loans. The second proposal addresses the public disclosure of HMDA data in light of consumer privacy interests.

In October, the CFPB expects to issue a final rule after the May 2019 proposed rule

With so many unexpected developments, it's nice when we have the opportunity to anticipate some of the changes that will require us to take action.

that would prescribe rules under Regulation F to govern debt collectors activities. The proposed rule would address communications connected with debt collection; and interpret and apply prohibitions on harassment or abuse, false or misleading representations, and unfair practices in debt collection. The CFPB did not announce when it plans to take final action on its supplemental proposal issued in March 2020, which addressed time-barred debt disclosures.

Finally, the CFPB considers a proposed rule that would offer a new "seasoning" definition of qualified mortgages (QM). This definition would create an alternative pathway to QM safe-harbor status for mortgages when the borrower has consistently made timely payments. This action would come on the heels of proposals to address the impending expiration of the Government-Sponsored Enterprises (GSE) Patch and will amend the General QM definition in Regulation Z to replace the debt-to-income limit with a price-based approach. The comment periods for the existing proposals close on August 10 and September 8, respectively.

The CFPB also discussed its participation in the interagency rulemaking processes to update the guidelines issued by Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). This partnership with the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Federal Housing Finance Agency is developing regulations to implement the amendments made by the Dodd-Frank Act to the FIRREA guidelines concerning appraisals. The changes require implementing regulations for quality control standards for automated valuation models (AVMs).

One of the items listed in the preamble to the CFPB's Spring Agenda that has not generated much attention is the agency's study of the impact of artificial intelligence (AI) in the context of Federal consumer financial laws and regulations. Banks raised issues related to AI in response to the CFPB's 2017 Request for Information Regarding Use of Alternative Data and Modeling Techniques in the Credit Process, the Bureau's 2018 Calls for Evidence, and other outreach since then. The Bureau continues to monitor AI developments and is evaluating whether rulemaking, a policy statement or other action may be appropriate. With the OCC's recent proposal regarding technological innovation, it would not be surprising to see the CFPB announce something on this topic in the near future.

To fulfill its obligation under Section 1022(d) of the Dodd-Frank Act, the CFPB is also conducting its five-year review of its Integrated Mortgage Disclosures Under the Real Estate Settlement Procedures Act (Regulation X) and the Truth in Lending Act (Regulation Z) Rule and certain amendments. The CFPB announced it plans to issue its TRID Rule assessment report by October.

The CFPB also expects to conduct an additional review under section 610 of the Regulatory Flexibility Act, which requires the Bureau to consider the effect on small entities of the rules it promulgates. The agency plans to review the Regulation Z rules that implement the Credit Card Accountability Responsibility and Disclosure Act of 2009.

Stay tuned to Compliance Alliance for announcements on these developments and more.

Chris W. Bell is an Associate General Counsel at Compliance Alliance. He has worked in the legal department of a federal savings bank and for the Texas Department of Banking. He is one of the C/A hotline advisors.

Foreclosure Protection: Where are We Now?

By Chris Bell, Associate General Counsel, Compliance Alliance

THE COVID-19 PANDEMIC HAS CHANGED American life as we know it. As the country continues to deal with the health crisis, the effects of containment measures ripple through the American economy. Unemployment remains high as state economies expand and contract in inverse proportion to the virus's spread. Regulators are in an arms race with rapidly changing markets, forcing banks to adapt to an ever-changing regulatory landscape. Even as we struggle to deal with the immediate concerns, we know the effects of this pandemic will be with us for some time. Economic shocks will continue to reverberate and play out in the housing markets around the country. As we shift into the next phase of operating in the pandemic and consider what options exist to help struggling mortgage borrowers, we should take note of the status of the expansive mortgagor protections passed by Congress, federal agencies and other government authorities.

Protection for Federally Backed Mortgage Loans

In the early days of the pandemic, Congress passed the Coronavirus Aid, Relief, and Economic Security ("CARES") Act. One of the primary sections of this law established a 60-day moratorium on foreclosure proceedings against homeowners with federally backed mortgage loans. The CARES Act's mortgage foreclosure moratorium applied to single-family residential mortgage loans secured, guaranteed, or made by FHA, USDA, VA, or Fannie Mae or Freddie Mac. Originally scheduled to expire at the end of June, the various agencies extended the moratorium on foreclosures and evictions until at least Aug. 31, 2020.

The CARES Act also granted Federally backed mortgage loan consumers experiencing financial hardship related to the COVID-19 pandemic, the right to request six months of forbearance (with an option of six additional months), regardless of delinquency status. Congress prohibited servicers from charging any fees related to this forbearance. Mortgage delinquency status is frozen in place during forbearance, even if the bank suspends payments during the forbearance. As it stands today, customers can request forbearance under the CARES Act until the earlier of the end of 2020, or the end-date of the national emergency concerning the novel coronavirus disease outbreak declared by the President on March 13, 2020, under the National Emergencies Act.

As with everything related to the COVID-19 pandemic, expect mortgage foreclosure protections to change as the county continues to deal with the long-term effects of our national crisis.

State and Local-Level Protection

Many state and local authorities enacted policies to protect mortgage borrowers and renters. The details of these state and local foreclosure bans vary. Banks should refer to the official websites for their state and local governments to assess the scope and requirements of applicable prohibitions. While effective dates vary widely, many of these protections remain in effect until respective governors lift statewide emergency declarations.

Private Loans

The CARES Act provided no relief for loans that are not federally backed. Banks should refer to the appropriate investor guidelines for mortgages sold to private investors. Banks should refer to guidance from its regulators concerning their expectations regarding non-federally-backed mortgage loans held in a portfolio.

Troubled Debt Restructuring ("TDR")

If neither a federal nor state moratorium applies to a residential mortgage held in a portfolio, you may still be able to exercise your authority to assist pandemic-effected borrowers who are struggling financially. Regulators have urged banks to work with customers and prudently modify loans in a safe and sound manner. Section 4310 of the CARES Act provided banks relief from TDR. In April, regulatory agencies issued revised interagency guidance to help banks sort modification requests into three groups: (1) loan modifications covered by Section 4310 of the CARES Act; (2) those outside of Section 4310 deemed not to be TDRs; and (3) those outside of Section 4310 that may be TDRs. In June, regulators released new interagency safety and soundness examiner guidelines. These guidelines instruct examiners to not criticize institutions for doing so as part of a risk mitigation strategy intended to improve existing loans, even if a restructured loan ultimately results in adverse credit classifications.

To be covered by Section 4310 of the CARES Act, a loan modification must: (1) relate to COVID-19, (2) be executed between March 1 and December 31 (assuming the current national emergency does not end earlier than the end of the year), and (3) the underlying obligation must be not more than 30 days past due. If a loan modification meets these three criteria, financial institutions do not have to report it as a TDR; however, the financial institution should maintain records of the volume of such loan modifications.

If a loan modification fails to meet any of the three criteria for Section 4310 coverage, it does not automatically result in a TDR. Regulators will deem a modification as not to constitute a TDR if it relates to COVID-19, extends no more than six months, and the underlying obligation is not more than 30 days past due. The only subjective criterion is the relationship of the modification to COVID-19. As a best practice, banks should have the borrower certify that the requested change is due to COVID-19. To not raise HIPAA concerns, the certification should be general and not address specific health details. While such a certification is not required to be in the loan file, it would show future examiners that the lender followed the guidance in good faith. If a bank receives a modification request that is outside the scope of Section 4310 and does not meet the described criteria, the bank should assess whether the modification would be a concession to the borrower that the bank would not otherwise consider and act accordingly.

As with everything related to the COVID-19 pandemic, expect mortgage foreclosure protections to change as the county continues to deal with the long-term effects of our national crisis. The federal agencies may extend the protections relating to the loans they back, and Congress will undoubtedly reassess the CARES Act's protections as the end of its covered period draws near. Despite how things change, you can count on the Arizona Bankers Association to bring you the most up-to-date information available as we walk hand-in-hand through this crisis.

Chris W. Bell is an Associate General Counsel at Compliance Alliance. He has worked in the legal department of a federal savings bank and for the Texas Department of Banking. He is one of the C/A hotline advisors.

PPP Fraud — How to Protect Your Institution

Fraud is something that bankers are always wrestling with, but these days, the Paycheck Protection Program (PPP) has given rise to a greater fraud opportunity. The PPP has radically increased the amount of lending to small and mid-sized businesses, with 5.2 million loans made as of August 8th. But the complexity of the application process and the goal of doling out money quickly have made it a prime target for fraud.

Even before the crisis, the results of an Aite survey of lenders who lend to small and mid-sized businesses turned up some troubling signs. While the percentages of suspected fraud were still relatively small, the bulk of lenders, almost a third of respondents, thought that between 0.11% and 0.5% of loans were being hijacked.

After the pandemic started, a former California banking commissioner, along with other experts, predicted PPP fraud rates could be 10 to 12%, which equals billions of dollars. This is a lot of money that won't reach businesses in need. "*History shows that when government relief programs are put together quickly in response to a disaster, fraud is fairly rampant*," notes Derek Cohen, a former federal prosecutor.

So, what are the areas that community financial institutions (CFIs) should pay particular attention to? As always, carefully and effectively identifying customers so that it is clear who is getting a loan.

New customers. Part of the problem in the PPP program is that there has been a rush of businesses trying to get the loans. While CFIs know their customers well, under PPP, you may have been asked to deal with new, first-time applicants who had to be vetted quickly. A fraudster could have snuck in, created a fake company identity, and gotten past the identification process to secure loan proceeds and disappear before alarms go off on the fraudulent activity. Being extra diligent about new customers is critical. You may want to review your new customer accounts to be sure all is in line to avoid future headaches.

Hijacked identities. It's not just new, first-time applicants that need to be closely watched, though. One of the tricks of the fraud trade is to hijack a real identity, in this case, masquerading as a small business customer already known by an institution to obtain loan proceeds illegally. This means paying special attention to irregularities even within your existing, loyal customer accounts.

How can you best protect yourself from PPP fraud besides carefully validating customer identities? Update anti-fraud analytics. Watch and continue checking for suspicious signs like phony addresses. Make sure fraud prevention and detection procedures are up-to-date. Keep current on the news from federal law enforcement on new fraudulent activity. Of course, have clear and effective responses when issues around applications arise too.

To fraudsters, periods of crisis represent an opportunity. So, CFIs will need to be especially vigilant in their fraud measures and customer vetting. We know you are fighting the tough fight for your customers out there. Keep at it!

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Dedicated to serving the needs of community banks, PCBB's comprehensive and robust set of solutions includes cash management, international services, lending solutions, and risk management advisory services.

Enforcing Loan Documents Amid the Pandemic and Related Economic Downturn

RICHARD HEROLD, JACOB SPARKS and W. BRIAN MEMORY
Spencer Fane LLP

THE COVID-19 PANDEMIC NECESSARILY EXPANDS THE LIST OF factors any lender must consider when enforcing the terms and conditions of its loan documents. There is a vast distinction between a corporate borrower who has looted the company and diverted corporate assets for personal gain and a corporate borrower whose business has been explicitly shut down by a gubernatorial pandemic order or forced into bankruptcy by a reduction or elimination or revenue. In short, a tailored approach to each borrower is always essential, but even more so now.

As borrowers struggle with reduced cash flows, depreciated collateral values, supply chain disruptions, changes in consumer shopping behavior, and new health and safety practices that constrain capacity and productivity, lenders will likely continue to receive a higher volume of borrower requests for forbearances, loan modifications, or other accommodations. When dealing with distressed borrowers, financial institutions must pursue proactive measures to assist their borrowers in finding stability and financial success, to protect the interests of the institution, and to preserve the value of the institution's loan portfolio.

When dealing with distressed borrowers, financial institutions must pursue proactive measures to assist their borrowers in finding stability and financial success, to protect the interests of the institution, and to preserve the value of the institution's loan portfolio.

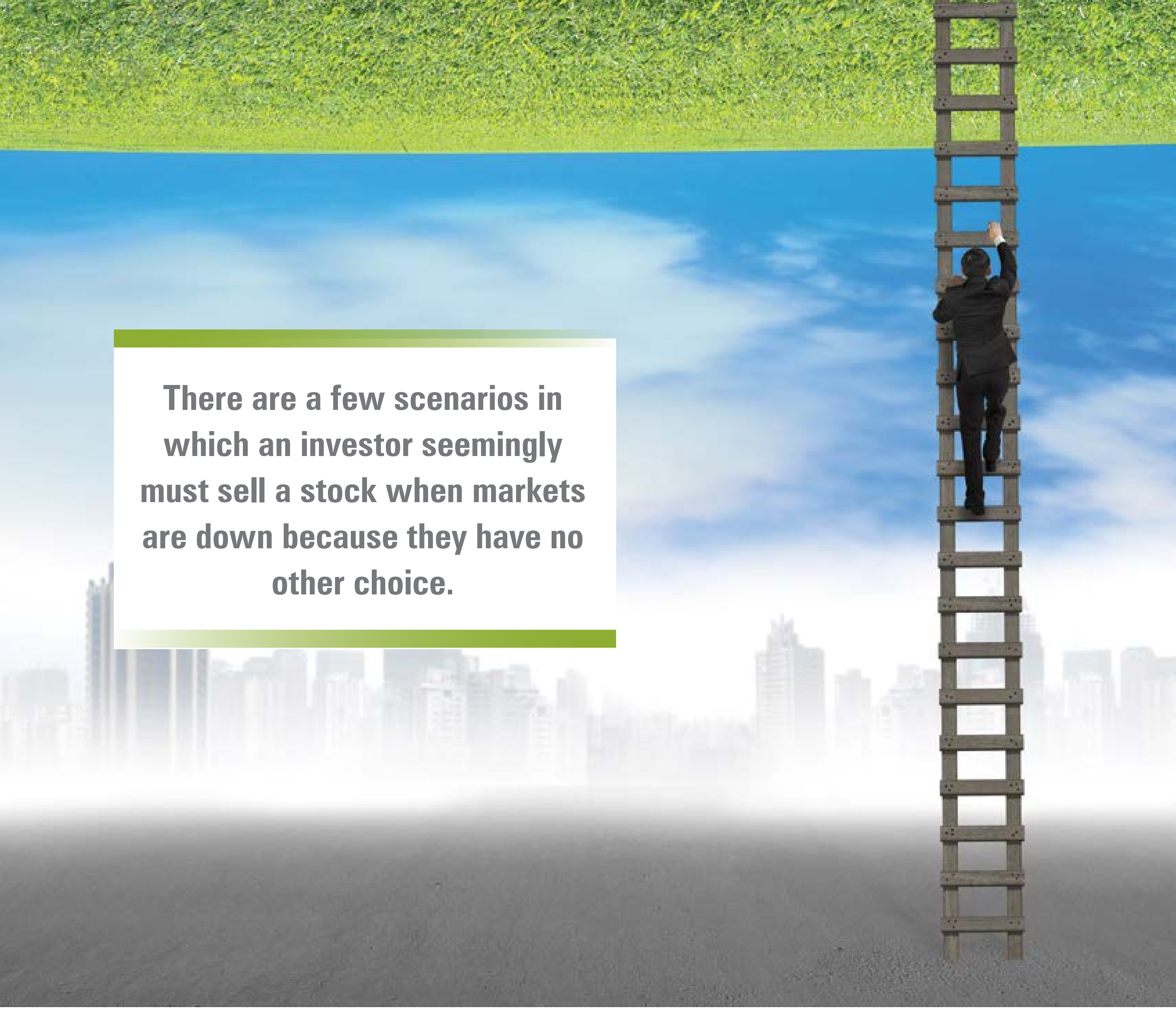
Reviewing the Loan Documents for Potential Deficiencies

Financial institutions should begin by collecting and reviewing all documents, including correspondence, relating to the loan. Documents should be preserved, well-organized and made easily accessible.

Lenders should confirm they have all required documentation and necessary signatures, and that the documents are otherwise free of errors or other deficiencies that could impact the financial institution's position. Workout situations provide an invaluable opportunity for the lender to resurrect missing documents, to cure document deficiencies and to address drafting errors.

Lien Perfection and Priority

A lien perfection and priority analysis is a critical part of any loan file review. This is a great time for the lender to confirm it has a properly perfected lien on collateral and its perfected lien is first in priority among any other existing creditors by reviewing the UCC financing statements to ensure the debtor's name is correct, the UCC-1 was filed in the proper jurisdiction and the collateral has been correctly described.



> There are a few scenarios in which an investor seemingly must sell a stock when markets are down because they have no other choice.

Entering Into Pre-Negotiation Agreements

Prior to engaging in workout discussions, financial institutions should consider entering into pre-negotiation agreements with borrowers and guarantors in which, among other things, they acknowledge any existing defaults and agree that no oral or written statements will be binding on any party unless a formal written agreement approved by the financial institution is formally signed by all parties. It must be clear in that pre-negotiation agreement that an exchange of emails is insufficient to bind the lender.

Analyzing the Terms of Any Loan Workout Agreement

Workout agreements — whether a forbearance, modification, deferral or other similar agreement — create an opportunity for the financial institution to make the best of what might otherwise be an unfortunate situation for all parties. Financial institutions have a vested interest in helping borrowers obtain stability and achieve financial success while protecting the interests of the financial institution.

Although there are a plethora of issues to consider and opportunities to achieve these goals, the following are highlighted:

1. **Information Gathering.** Lenders should use this opportunity to gather as much current data as possible. A field audit of current inventory, accounts receivable, and equipment is prudent to obtain current valuations of collateral and to verify the accuracy of the borrower's reporting. The information-gathering may also help the financial institution recognize strengths or weaknesses in the borrower's business, its management team or its industry

The financial institution might feel more comfortable making certain accommodations to the borrower in exchange for additional collateral.

generally. For example, has the entire industry been shut down by an explicit gubernatorial order, precluding any revenue?

2. **Additional Collateral.** The financial institution might feel more comfortable making certain accommodations to the borrower in exchange for additional collateral. When available, a lender can obtain liens on unencumbered assets or second liens on encumbered assets. If the lender takes a lien on encumbered collateral, an intercreditor agreement with the other lienholder may be a useful step.
3. **Pledge Agreement.** If the borrower is a partnership or limited liability company, the lender should assess the desirability of requiring an equity interest pledge. Likewise, if the borrower is a corporation, the lender should consider requiring a stock pledge. In either situation, experienced counsel can help the lender perfect a security interest in the pledged collateral.
4. **Deposit Accounts.** If the lender is not the bank with which the borrower's deposit account is maintained, the lender can obtain control of the borrower's deposit account through a deposit account control agreement. If a default occurs later, the lender will then be able to instruct the borrower's bank to pay the balance of the borrower's deposit account to the lender.

Litigation of the Issues

Despite the lender's best efforts, it may become necessary to litigate by (1) seeking to appoint a receiver to protect and preserve the collateral, (2) pursuing a trustee's sale, (3) conducting a fair market value hearing to address the amount of the deficiency due and owing to the lender, or (4) defeating any counterclaims asserted by the borrower or guarantors. This can and should be a professional and orderly process, yet frivolous (and occasionally well-founded) affirmative defenses and counterclaims can delay interim judicial decisions and the final resolution of the case.

There is, of course, no reason to spend a great deal of time and money litigating the issues if the defendants will not be able to satisfy any judgment. Ask for an affidavit of financial condition, cross-check it with

During challenging economic times, financial institutions need to work proactively with borrowers on commercial loan workouts that are, to a degree at least, of value to both the institution and the borrower.

an independent asset search, and let the lender make a business judgment on the value of continued litigation.

And don't overlook the value of mediation. Sure, it is a meaningful investment, but the case may be resolved, with finality, by the consent of the parties, in the course of one day, rather than over the next 12-24 months.

Chapter 11 Reorganization under the United States Bankruptcy Code

Ultimately, some borrowers will seek protection under the United States Bankruptcy Code. A predictable effect of the economic devastation wreaked by the coronavirus is that bankruptcy filings are on the rise, and lenders need to be aware of how the Small Business Reorganization Act of 2019 (SBRA) will change the bankruptcy landscape in certain Chapter 11 bankruptcy cases. The SBRA is a new debtor-friendly fast-track bankruptcy option that will alter the dynamic of negotiations between banks and their small business borrowers who file bankruptcy under Chapter 11.

The SBRA went into effect in February 2020 and modified traditional Chapter 11 practices and procedures with the intention of creating a faster, more efficient Chapter 11 process for small business debtors. For example, the SBRA requires debtors to attend a case status conference within 60 days and file a plan within 90 days. At least 14 days before the status conference, debtors are required to file a case status report detailing the debtor's efforts to obtain a consensual plan. Debtors are not required to file a separate disclosure statement, but the plan must include a brief history of the debtor, a liquidation analysis, and financial projections relating to the debtor's ability to make payments under the proposed plan of reorganization.

It is worth noting that debtors whose entire industry has been shuttered by the orders of state governors have had success asking for more time to propose a plan of reorganization on the theory that neither any financial projection nor any reorganization plan can be generated until revenues return.

Perhaps the most notable characteristic of the SBRA is that it allows, under certain circumstances, a debtor to "cram down" a non-consensual plan of reorganization. Under the SBRA, only the debtor can file a reorganization plan, and the court can confirm a debtor's plan without the support of any class of claims as long as the plan is deemed to be fair and equitable with respect to each class of claims and does not discriminate unfairly.

Furthermore, the "absolute priority rule" does not apply to SBRA cases. Typically, when a Chapter 11 plan does not propose to pay creditors in full, equity owners lose their ownership interest unless they provide new value to fund the plan of reorganization. The SBRA, however, allows for confirmation of a Chapter 11 plan that maintains pre-bankruptcy ownership while discharging the reorganized debtor's unpaid debts, as long as the debtor's plan meets the SBRA's plan confirmation requirements. To offset this advantage, lenders should consider taking a lien on owners' equity as part of any pre-bankruptcy workout agreement.

Because plans of reorganization under the SBRA may only be filed by the debtor, can be confirmed without any class of creditors voting in favor of the plan, and are not subject to the absolute priority rule, prepared debtors with valuation evidence and financial forecasts may be able to quickly confirm a "cram down" plan. Therefore, lenders confronted with SBRA cases must be prepared to act quickly to engage counsel, participate in negotiations with the debtor and trustee to explore the terms of a consensual plan, and to establish and defend the bank's claims and liens.

Conclusion

During challenging economic times, financial institutions need to work proactively with borrowers on commercial loan workouts that are, to a degree at least, of value to both the institution and the borrower. In doing so, lenders should take the opportunity to analyze loan documents, identify potential issues, and strengthen the lender's position during the workout process. To the greatest extent possible, lenders should also use the workout process to obtain or to replace missing documents, cure document deficiencies, fix drafting errors and obtain additional security. Finally, if a borrower files bankruptcy under Chapter 11, the lender needs to be aware of recent changes brought about by the SBRA and act quickly to protect its rights.

FinTech Lending Q1 and Q2 2020

CHAPTER I. FINTECH

FinTech lending originated and has become popular in the United States and around the world in the 12 years since the 2008 financial crisis. FinTech innovators saw a need when larger banks reduced consumer lending and filled the void to provide financing. One of the main reasons behind the success is the digital setup of the marketing, underwriting and funding processes. The critical point of the online lending concept is to attract as many consumers and small to medium-sized businesses as possible by campaigns over the internet, social media, and emails. Utilizing the main advantage of lending — a product everybody wants — money helped to attract demand combined with a technology-based, online culture. In many cases, the campaigns are not focused on the loan itself but rather focused on the new utility or product that is now closer to the borrower through the loan. Each and every campaign is measured by utilizing different funnels, matrixes. The analysis of the lending process is optimized over different channels add more and more visitors to the webpage. Fintech has always been prepared to pay for that Facebook click and credit reporting lead.

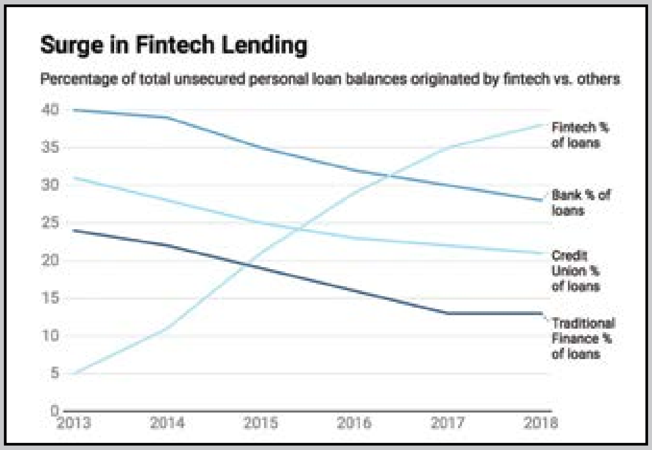
Fintech's initial focus is to attract as many visitors to the webpage as possible, having led 1000s of views and direct borrowers directly to the application. Potential and current borrowers are not shown a fancy company webpage or complex information. The objective is to make the click to an application as simple as possible.

CHAPTER II. APPLICATION

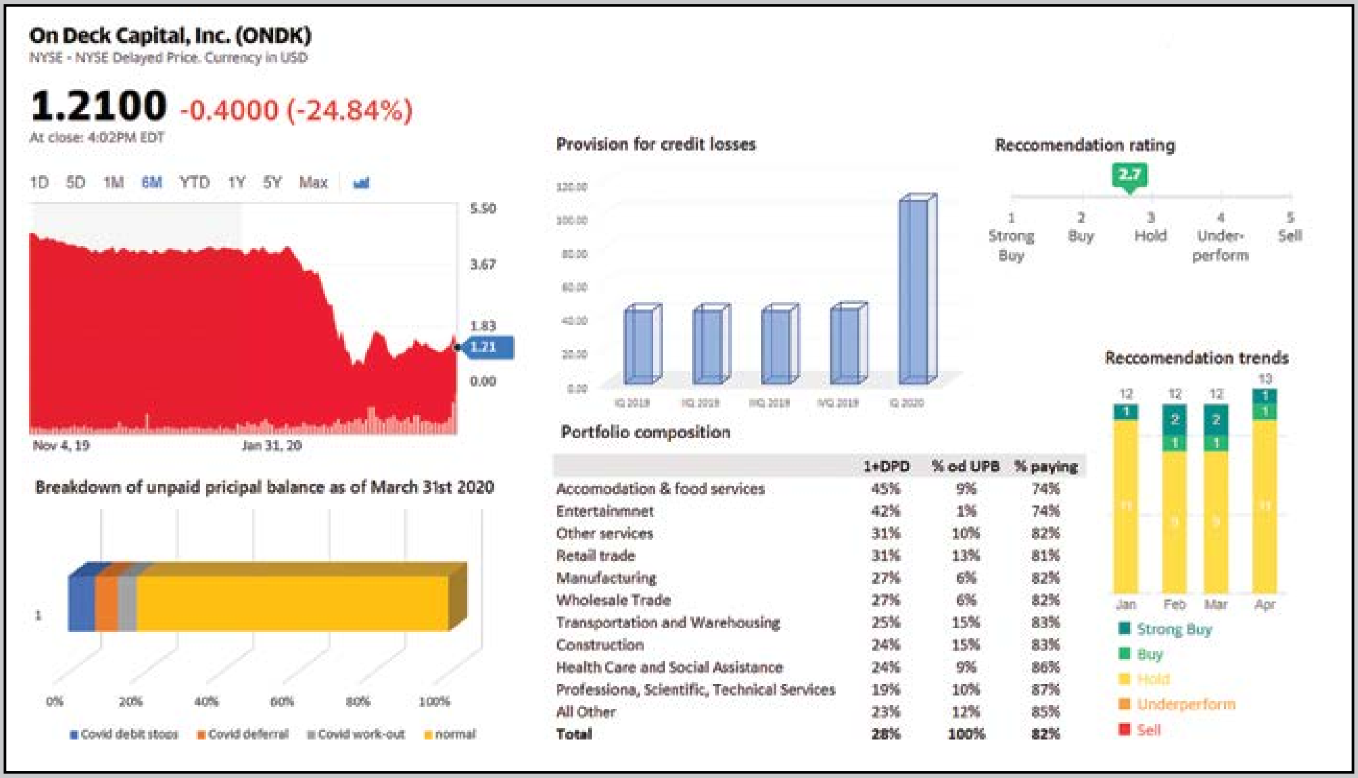
The application process on the Fintech Lender's webpage is again optimized. What information do we need to know first, save the data, and then have the consumer proceed to the next page? Attract consumers to the amount of money they may apply for at an attractive rate, obtain the name, phone number, email and click next. Once the borrower does not continue the application, he may be contacted and asked if he needs assistance. This technology needs to be optimized and improved to facilitate the progression of the lender.

CHAPTER III. UNDERWRITING AND VERIFICATION

The Underwriting process is the next step. Underwriting starts with gathering the data required to evaluate risk and to make a sound decision. Engaging the borrower to be attracted to the process and motivated to move to the next step is critical. It is important to simultaneously make the process interesting to the consumer and to verify the details provided on the application are correct. Verification may be completed internally or by an external provider. Examples of fraud prevention analytics measure the time to enter a birthdate, how many times the name has been rewritten, asking the borrower to connect their bank account and additional information. In addition, complete a review to ensure the borrower is not stacking loans (other Fintech lenders providing loans to the same borrower concurrently.)



OnDeck Capital on April 30, 2020 after the IQ numbers announced.



CHAPTER IV. NUMBERS

The Underwriting process had always been a challenge for Fintech lenders. Non-performing loans and the definition of NPL is not 100% aligned with best practices in the banking industry. Sometimes Fintech is viewed as more Tech (technology) than Fin (finance). One reason for this is attracting consumers with proper marketing and technology to apply for loans. Build the book if you will, and initially focusing on the process before risk. The concept of quick, reasonably priced processes with employees motivated by technology, relaxed culture and measurable criteria allowed the companies to attract a lot of interest from investors. Lenders considered this relatively low cost to obtain a loan as costs incurred with creating innovative technology to approve loans and retaining a performing part of the portfolio within the Fintech lender.

[redacted]

On Deck Capital, Inc. (ONDK)
NYSE - NYSE Delayed Price. Currency in USD

0.6118 -0.0502 (-7.58%)
At close: 4:00PM EDT

market capitalization: 35.744M
Beta (5Y Monthly): 1.58
52 Week Range: 0.5400 - 4.7400

Performance Outlook

Short Term 2W - 6W | Mid Term 6W - 9M | Long Term 9M+

[redacted]

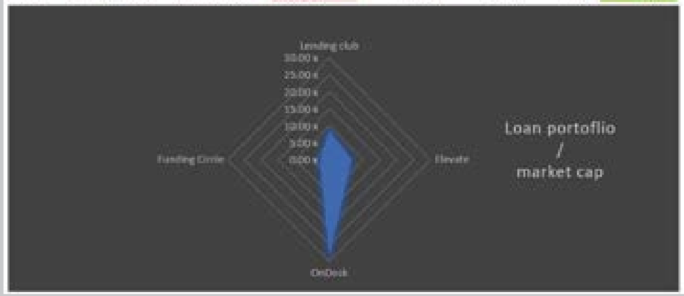
		March 31, 2020
Assets		
Cash and cash equivalents	$	121,148
Restricted cash		29,094
Loans and finance receivables		1,291,586
Less: Allowance for credit losses		(205,703)
Loans and finance receivables, net		1,085,883
Property, equipment and software, net		23,714
Other assets		77,339
Total assets	$	1,337,178

[redacted]

[redacted]

Different FinTech lenders by the end of June 2020

Symbol	Company (short)	Current price	Change day%	Change since Feb20	Average Volume (3M)	Market Cap	Portoflio size	Portoflio / Market Cap
LC	Lending club	$4.89	-2.30%	-62.64%	1.242 M	339 M	2784 M	8.21 x
ELVT	Elevate	$1.91	-0.26%	-51.65%	0.493 M	81 M	516 M	6.37 x
ONDK	OnDeck	$0.82	-6.16%	-80.57%	1.903 M	48 M	1304 M	27.17 x
FDCHF	Funding Circle	$0.94	-9.17%	-15.32%	0.000 M	331 M	906 M	2.74 x



One of the factors by FinTech lenders that influenced their performance has been rollover from DPD 5 (5 days overdue) to DPD 30, then DPD 30 to DPD 60, DPD 60 to DPD 90, DPD 90 to 180 and charge-off. The charge-off ratio did not, initially, impact the lender's valuation. In the growth stage, they calculated the number of loans getting to charge-off in comparison to the entire loan book. As lenders reached the stratosphere of maximum market penetration, the actual charge-off % did start to show. As many of the loans are not collateralized, the value of collateral did not allow to decrease the value of LGD. EAD (exposure at default) has dramatically increased as well, due to collection processes being impacted both internally and externally. A lack of resources, appetite and experience handling of collection accounts led to increases in delinquent accounts. Bad data entry, setup of legal agreements and lack of desire to pursue a judgment limited success on recovering principal on defaulted loans. Many judgments, if obtained, had been on a default judgment basis in the state of the legal department of the Fintech lender to both decrease costs and presumably to initiate payment discussions. Filing all judgments in the state of the lender would result in limited enforcement options of the judgments.

FinTechs also encounter different modes of fraud. If the fraud is occurring due to an invalid or third party SSN, the fraud is likely happening by repeat professional borrowers, or a borrower with no intention to repay the loan. Loans have been provided to borrowers to finance bankruptcy; loans without requiring an SSN or loans to small business, such as restaurants, have added additional risk to the business.

On the side of the revenue, FinTech is less regulated than a bank or credit union. One extreme example is a Title Loan company. They have the ability to receive revenue from the purchase, underwriting costs, servicing fees and ability to refer new services to clients to supplement the non-performing loan book.

Additionally, the constant change of Chief Risk Officers (usually every two years), different interests of boards in disagreements with investors over performance, and vision and pre-IPO valuation linked to the loan book had been a challenge.

2020 IIQ CHAPTER V.

The second quarter of 2020 was the most challenging quarter in FinTech lenders' lifecycles so far. There had been no financial crisis since 2008, and all the models will show the performance only in a good economic market. Publicly traded companies did publish financial numbers of Q1 2020 around April/May 2020. There was numerous information reported to read, comprehend, and draw conclusions from. The amount of loans being on work-out and the amount of loans not paying were daunting for a partial quarter impacted by COVID-19. Technical analysts at many equity trading platforms as Yahoo! Finance and others did not fully understand what was happening and recommendations to hold or buy seemed out of place, even at the time. Fundamentals did change.

OnDeck results of IIQ 2020

ondeck

IIQ 2020 Financial results notes

1. The 15+ Day Delinquency Ratio increased to 39.5% from 10.3% the prior quarter
2. Peak of 42% in May
3. 1+ Day Delinquency increased from prior quarter peak of 47% in May to 43% at June

In the end, the final selling price of OnDeck was $90 million, $8 million of which was paid in cash, with the remainder paid in Enova stock.

A very similar company to OnDeck named Kabbage (in terms of portfolio size) had been sold for around 800 million USD without the portfolio.

Name: Kamil KNAP
Position: president and director
Company: EPA USA Inc.
Education: Stanford University, City University of Hong Kong, Masaryk University

Name: Ryan SESTER
Position: CEO
Education: Arizona State University

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