Multi-Lender Securitization Program of Unguaranteed Portions of SBA 7(A) Loans

- Creating a Level Playing Field for CDFI, MDI, Credit Unions and Community Banks
- Focus on Low and Moderate-Income Communities, Underrepresented Business
- Expanding SBA's Lender Base

FALCON BRIDGE Capital

June 30th, 2023

Executive Summary

Objective: Multi-participant program will allow more than one SBA lender to pool their Unguaranteed Portions of SBA 7(a) loans into one transaction. Under SBA 13 CFR §120.422, SBA will consider securitizations involving multiple lenders on a case-by-case basis, using the conditions in § 120.425.

Summary:

1. Existing regulations have enabled select non-depository institutions under SBA 13 CFR §§ 120.420 - 120.425 to securitize unguaranteed portions of 7(a) loans.

2. A multi-participant program will allow CDFI, MDI, and SBA lenders of all sizes to collectively access capital markets as a source for non-recourse funding without sole dependence on local deposits.

3. Higher interest rates are forcing depository institutions to compete for deposits with other investment vehicles making it inefficient to fund SBA 7(a) loans.

4. By allowing a multi-participant securitization, lenders will have an additional tool to achieve desired risk management, liquidity, and capital efficiency to further aid small businesses in their respective communities.

5. Due to high set-up costs associated with creating a complex bankruptcy remote Securitization Trust to issue Notes to interested bondholders, only a few institutions have been able to utilize the program since its authorization; according to the final rule effective April 1999.

6. Government Accounting Office study in 1999 highlighted the benefits of capital markets and discussed issues with regards to limitations of a single bank being able to create an efficient secondary market for unguaranteed portions of SBA 7(a) loans. https://www.gao.gov/assets/ggd-99-64.pdf

7. A multi-lender securitization program will indirectly expand SBA's lender base and reduce reliance on local bank deposits to fund SBA loans.

8. **Borrower Impact:** Creating more efficiencies for SBA lenders, will allow SBA to increase its flagship 7(a) lending programs to underserved communities and businesses.

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Benefits: Securitization of the Unguaranteed Portion of SBA 7(a)

Community Bank/Other Non-Depository Lenders	Borrower	SBA
✓Frees up liquidity for more lending ✓Frees up Capital and Loan loss Reserves on existing loan portfolio. Avoid shareholder dilution ✓Reduces reliance on local deposits to fund 7(a) loans ✓Risk Management – Ability to manage concentration build-up ✓No disruption in lending to borrowers due to concentration limits ✓Added capacity increases profitability over the long-run	✓Access to capital needed to start, operate and expand business. ✓Maintain relationship with existing bank ✓Benefits from lower cost of funds through securitization economics ✓Expanding capital access for small business borrowers recovering from the pandemic	✓Access to liquidity through capital markets ✓Does not rely solely on banks funding loans with local deposits ✓Risk exposure is diversified from FDIC Insurance fund to private capital ✓Leverages existing lending processes to borrower through regulated community banks and other non-depository lenders while accessing additional private markets liquidity

Expansion of the Existing Securitization Program

Objective: **Create a multi-participant securitization program under the existing SBA regulations to allow multiple lenders to pool their unguaranteed portions of SBA 7(a) in the same transaction.**

- The multi-participant platform will enable smaller SBA Lenders to collectively access capital markets and achieve desired risk management, liquidity, and efficient use of capital to further aid small businesses in their communities.
- This will directly support development, growth and health of small businesses across the country, **without the additional exposure to the taxpayer.**

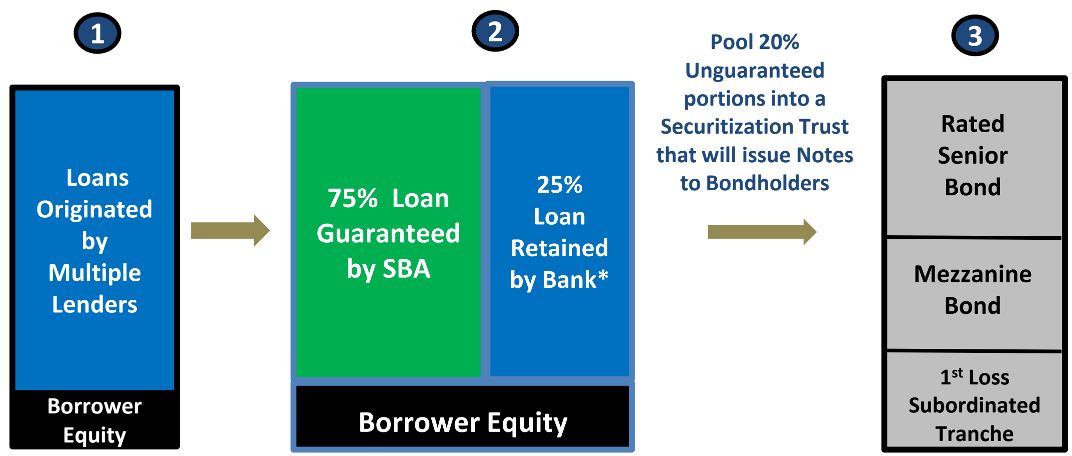
Applicable Regulations: Under SBA 13 CFR §120.422, SBA is allowed to consider securitizations involving multiple lenders on a case-by-case basis, using the conditions in § 120.425.

Existing Program Description:
SBA Secondary Market Program was established as "the primary liquidity channel" available to SBA lenders. It allows the sale of the Guaranteed Portion (75% of the loan) in the secondary market and provides guidelines for securitizing the Unguaranteed Portions (up to 20% of the loan).

Existing Program Limitations:

- Due to high costs and lack of economies of scale, only a few individual SBA lenders have been able to securitize unguaranteed portions of 7(a) loans.
- Smaller SBA lenders, community banks, and especially those located in rural and minority communities, have been shut off from participation as they individually lack sufficient loan volume and expertise to execute an efficient securitization.

A multi-Lender securitization will attract investors with varying risk appetite to fund SBA Loans:



* Up to 20% Unguaranteed portions will be pooled in a Special Purpose vehicle ("SPV") that will issue rated and unrated securities to fund the loan portions on a non-recourse basis; thereby freeing up liquidity for lenders to expand additional lending in their communities.

Continued Risk Management and Oversight

Risk Management Designed to Eliminate Excessive Risk Transfers

1. Loan Seasoning: Banks will be required to hold unguaranteed portions of loan on balance sheet for a minimum of 6 months before selling into the program. Exception to be made by Deal Manager for meeting liquidity needs of specific lender.

2. Loan Guidelines: Specific loan underwriting guidelines and minimum financial metrics to be required by Securitization Deal Manager. Excessive risk can not be transferred to Securitization Trust.

3. Bank Loss Performance: Historical loss performance will be the criteria for participation. SBA guidelines exists for institutions seeking securitization approval. **Bank must be classified as well-capitalized by Bank Regulator.**

4. Reps & Warranties on 100% of Loan: Banks will be required to provide Reps & Warranties on loans being sold into securitizations. *Early-Pay Default provision required.* ***Lender is already providing Reps and Warrants on its 75% Guaranteed Portion.***

5. 3rd Party-Loan Review: Assembler / Deal Manager will sample review loans to ensure SBA and individual lending guidelines are met.

6. Existing Regulatory Oversight: All participating banks need pre-approval from SBA for participation.

7. Risk Retention: Lenders will still have “skin in the game” after securitization. SBA risk retention requirements and Dodd-Frank risk retention rules to apply for all participating lenders in Securitization.

The Expansion of the Securitization Program Will Not Result In Increased Risk-Taking

1. SBA’s internal PARRiS methodology for oversight of SBA Lenders will prevent any change in risk-taking behavior.
2. Lending institutions participating a multi-lender securitization program are mostly regulated by banking authorities that include FDIC, OCC, State Banking Departments.
3. Additional due diligence from Rating Agencies(Standard & Poor’s, KBRA), Underwriters, Placement Agents, and Bondholders to ensure NO excessive risk transferring.
4. Risk management is a key metric for all insured institutions and a requirement for internal Board and Management.
5. SBA loan loss performance has been historically low relative to other asset classes. Lending origination processes and risk management not impacted by this proposal.

Program Design Underway with SBA's Office of Capital Access – Target Execution Week of Sept. 18th , '23

	Target Dates
Bank Participation Approval **Frequency of Offering:** a. Initial Transaction Focused on CDFI, MDI, Community Advantage Lenders, Credit Unions, and Community Banks. b. Programmatic approach to offer two (2) to three (3) securitization transactions per year.	Loan Pool Finalization ~July 31st
Eligibility Guidelines a. Loans must be fully funded. b. Loans must be current at the time of sale to securitization Special Purpose Entity ("SPE"). c. Loans must be 12 months or more seasoned, (exceptions to be approved by securitization investors). d. All loans must meet eligibility criteria of SBA SOP 50 10 5	Completed
Securitization Counter-Parties a. Guidehouse to continue as Fiscal Transfer Agent for new securitization platform. b. Morgan Lewis, Blank Rome, SEC and Regulatory Counsel, c. Indenture Trustee TBD, d. SBA Continues as Master/Backup Servicer	Completed
Legal Structure / Reps & Warranties /Risk - Retention a. Securitization structure to comply with SBA's Multi-Party Agreements applicable to all securitizations of SBA 7(a) loans. b. All participating lenders to provide Reps & Warrants and comply with all SBA and SEC Risk Retention Rules.	July 2023
Underwriting & Due Diligence a. Statistical Sampling for FDIC-Insured depository institutions	June – August 2023
Placement Agent & Investor Roadshow a. Transaction Term Sheet b. Underwriters counsel and PPM to be finalized with Deal Counsel c. Investor Presentation d. Roadshow	September 2023

Company Background

INVESTORS

Capitalize on FBC's insight and product knowledge of the U.S. Securitized market

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