

Clarification of the treatment of security under the Enterprise Finance Guarantee

Since launch of the scheme on 14th January 2009, anecdotal evidence has suggested that lenders are interpreting the scheme rules around the taking of security in different ways. This note seeks to clarify the way in which Government envisages the taking of security under the Enterprise Finance Guarantee to work in practice. In summary:

- If a lender determines that a borrower has access to any security available in a principal private residence but chooses not to take a charge over the property then that decision does not preclude the lender from making an EFG loan.
- However, EFG is not a mechanism for putting beyond consideration any asset which, according to normal commercial lending criteria, might be considered available as security.
- An existing loan may not be refinanced with a new EFG-backed loan for the purpose of releasing the security previously provided.

Lending under the Enterprise Finance Guarantee (EFG)

Lending under the Enterprise Finance Guarantee (EFG) is delegated to the participating lenders (latest lender list attached) and is made available as an extension of their commercial decision to lend.

That means that the lending decision will rest primarily on the lender's assessment of the borrower's ability to service the loan. The lender will also take into consideration the level of financial commitment of the individuals controlling the business. This is because it has been shown that the risk of default dramatically decreases when an individual has a material stake in the loan. It is critical, therefore, that they have some "skin in the game".

If the borrower is able to service the loan and is able to provide sufficient security then there is generally no need for EFG to be used. However, if the borrower has insufficient or no security, or if there are other factors affecting the lender's willingness to lend, then EFG may provide the means to make lending possible.

The Enterprise Finance Guarantee may be used to enable three types of lending:

- a new term loan, either unsecured or partially secured;
- a new term loan specifically for the purpose of transferring long term debt out of an overdraft in order to release capacity in the overdraft;
- the refinancing of an existing secured loan which would otherwise be withdrawn due to deterioration in the quality of the security.

Using EFG where there is no available or insufficient security

If the lender deems the borrower to have no or insufficient security available, then EFG may be used. In the event that a Lender determines that a borrower has access to security available in a principal private residence, but chooses not

to seek a charge over the property, then that decision does not preclude the lender from making an EFG-backed loan should they consider it appropriate to do so.

In this case, the lender may take an unsupported personal guarantee from the borrower and, where it constitutes tangible but nevertheless only partial security, the lender may also or alternatively take a direct charge over a specific business asset.

Any unsupported personal guarantee taken must exclude any entitlement to take a direct charge over the principal private residence of the borrower. The level of the unsupported personal guarantee is at the lender's discretion.

Taking security when releasing overdraft capacity or refinancing existing debt

In cases where EFG is being used to transfer existing long term debt from an overdraft into a new term loan or for refinancing, any security which had previously been provided in connection with the granting of the original overdraft or loan must remain in place.