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CHARTERED ACCOUNTANTS

YOU & YOUR BANKERS

One of a series of business
advisory publications
available on request

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The information presented in this brochure is necessarily of a general nature and should not be relied upon as a substitute for specific advice. For advice on, or assistance with any of the matters raised, please contact;

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Which One and Why

The deregulation of the financial sector has allowed additional banks to operate in both the retail and wholesale markets.

A banker's function is to provide custody of funds which are not immediately required.

Profits are generated from the successful and secure lending of such funds and arise from the margin between lending and borrowing interest rates, less the cost of operating, and including any lending losses.

Consideration should be given to:

- The image of the Bank
- The range of services available
- Existing relationships
- A professional relationship

The Image of the Bank

It is the custodian of your money so consider:

- Who owns it?
 - Is it listed on the share market?
 - How has it performed?
 - Is it basically New Zealand or overseas owned?
 - Does it benefit the community?
- Have the owners supported it in a time of need?
- Has it led or followed behind other financiers with changes in both deposit and lending interest rates?
- Are the services aggressively marketed? If so, why?
- Is your reaction favourable or unfavourable?
- Is the number of branches expanding, declining, consolidating, or remaining static?
- Does it have a reputation for
 - Providing reliable and efficient service?
 - Making decisions quickly?
 - Honouring commitments?
 - Being quick to "pull the plug" when things are not going too well?

- Being approachable?
- Frequently changing the local manager or branch staff?

The Range and Cost of Services Available

Determine

- Whether or not each account is basically a “depositor” or “borrower.”
- Whether or not you wish to be “a big fish in a little pond” (bank locally) or “a little fish in a big pond” (bank at a major city branch).

Consider

- Is the branch location convenient?
 - Is free vehicle parking available?
 - Are teller facilities to be used?
 - Are teller facilities adequate or are there often long queues?
 - Are such queues of concern?
- Do staffing levels appear adequate?
 - Is prompt service available?
 - Are queries dealt with promptly and efficiently?
- What services are required?
 - Cheque accounts
 - Interest bearing accounts
 - Safety deposit facilities
 - Foreign currency accounts
 - Importing and exporting assistance
 - Money machines
 - Lending services
 - Credit cards
- What are the costs of such services?
 - Base account fees
 - Activity fees
 - Clearance fees
 - Cash handling fees
 - Base interest rates
 - Is interest paid on cheque accounts?

Other Existing Relationships

Determine

- Whether or not there are any family associates with any bank or branch?
- Are such associations an advantage or a disadvantage?
- Are business associations with any bank or branch an advantage or a disadvantage?
- Whether or not business and personal accounts are to be maintained at the same bank or branch?

A Professional Relationship

Your bankers must be professional in their approach for they are the caretaker of your funds just as your doctor; dentist or surgeon is the caretaker of your health.

Your relationship must be based upon mutual trust.

Your Relationship – Is it Good or Poor?

Because a bank is a corporate creature, each staff member has a defined role and limitations on his/her authority. Find out who is responsible and who has authority to deal with your requirements.

Should the service given not be of a professional standard, discuss the position with the Branch Manager, and only change branches and banks if satisfaction is not then obtained.

Some Dos and Don'ts

Do

- be honest
- be reliable
- be realistic
- be consistent
- be punctual
- be meticulous in observing credit limits
- be good at communicating
- keep the banker informed of

- the activities undertaken even where the account operates on a credit basis
- seasonal fluctuations which are foreseen
- problems which are foreseen, and the actions which are to be taken to solve them
- ascertain when your credit limits are due to be reviewed and advise your Chartered Accountant accordingly
- co-operate with your Chartered Accountant to ensure that the required information is available to complete your financial statements in adequate time.

Do Not

- be dishonest
- be unreliable
- be unrealistic
- be inconsistent
- be uncommunicative
- ignore agreed credit limits
- ask for too much credit or for more than you really need
- accept income tax advice from your banker
- accept your banker's advice as to where new loan proceeds should be deposited and where subsequent repayments should be made from without checking on the income tax implications.

Your Loan Application

In every lending proposition, the basic ingredients of

Character
Capacity
Capital
Collateral

And will be assessed against the

Personal factor
Purpose of the loan and priority
Payment or repayment
Protection or security
Perspective or overview

Personal Factor

Banks lend to people. The personal factor is the prime consideration in any lending proposition and it is the one essential ingredient which must be “right.”

Even when lending to companies it is the integrity and abilities of the Directors and Management that first come under scrutiny.

The reliability, commonsense approach, and experience will all be carefully considered in making the assessment of the personal factor.

The borrower must also convince the banker that the financial affairs and accounting function of the business are in capable and trustworthy hands and that the prospects are such to give a feeling of confidence and optimism.

The loan proposal must clearly demonstrate:

- that the borrowers know and understand what they are doing
- that the business is run efficiently
- that empty promises are not given.

The banker must be advised of important matters affecting the business and these should not be withheld until the banker asks for the information.

No prudent banker will become involved in a lending proposition if the personal factor looks unsatisfactory at the outset.

Purpose of the Loan and Priority

This is generally considered together with the priority of the request, for any applicant will undoubtedly consider that their request is of the highest priority.

The banker needs to assure themselves that:

- the purpose is legitimate
- the loan sought is of benefit to both the borrower and the bank
- the request is appropriate to bank lending which is basically short to medium term

Bankers do not lend on poorly planned or ill-conceived projects. They are very wary of taking over loans from other banks or lending institutions and they are reluctant to bail out creditors.

Payment – or Repayment

When a bank grants a credit limit or a loan it expects that the arrangement will be observed. The customer must, therefore, demonstrate that they can meet the obligations with reliability, and preserve their reputation.

Accurate and realistic cash flow forecasts, which demonstrate that the project is viable, must be presented with a loan application to demonstrate that repayment or a reduction programme can be achieved.

Assessment of profitability and forecast closing balance sheets, together with notes detailing the underlying assumptions, should generally be presented in support of the application.

The bank may, in some cases, require regular reporting on the actual progress achieved and its comparison with the forecasts initially supplied. This may mean that a business is required to account for variances at a much earlier time which may, in some cases, save the business and lead to action being taken to put it on the right track.

A customer who has always done their best to meet the agreed obligations, and who has been completely honest and frank with the bank will receive fair consideration of their proposals.

Protection or Security

Security is the protection taken to make a loan safe. It is the protection and sometimes the final way out that a lender needs. Nevertheless, a banker will not lend if it appears likely they will have to realise on the security. Realisation is the absolute last resort.

The proposition must be sound before the question of security is considered. For good security does not of itself make a loan satisfactory.

Bankers are wary of customers who say “How much will you lend me on this security?” for it indicates a complete lack of understanding of the nature of lending and the needs of the borrower.

Very conservative values will be attributed to the assets involved for experience has proved that anything sold under forced sale conditions realises much less than expected.

Guarantees are the easiest of documents to sign but are the hardest to enforce. An unsupported guarantee, even from a person of considerable wealth, can be difficult to collect. Few people signing guarantees really know what they are signing and even fewer think that they will ever have to pay, but with every guarantee there is a legal obligation to pay if the principal debtor defaults.

Guarantees are necessary in some cases and are essential from a banker’s view when lending to a private company where the security is a debenture over the assets involved.

Guarantee your company’s borrowings but never give a guarantee in respect of a third party.

If the only strong point of a loan proposal is security then it should probably be declined.

Perspective or Overview

This includes all and any other relevant factors which may have a material bearing on whether the loan is approved such as:

- the history of relationships
- have past arrangements been kept?
- have cheques been issued in excess of arrangements?
- does the applicant and his family support the bank? Should they?
- where do deposit funds go?
- does the customer chase high interest rates with the bank’s competitors?
- what other bank services are used?

The banker must be kept informed and must have confidence from all cards being laid on the table. Problems and troubles will arise if a customer attempts to deceive his or her banker.

Keep the bank advised of progress and let the banker do some of the worrying. They might not like it but will appreciate being kept informed.

The following will always be considered:

- The people involved (the personal factor)
- The financial stability of the applicant
- The capacity to service the loan and adhere to arrangements
- The history
 - borrowing record
 - deposit support
 - past and future
- Planning and prospects
- Priority of the loan
- Is the request and repayment programme realistic?
- Has the proposition been well submitted with all facts and information available?
- What equity is the applicant contributing?

Your Application

A well prepared application will markedly increase the chances of success, and may even result in a lower interest rate.

Give the banker ample time to make a decision and do not insist on quick answers. To do so will almost certainly bring a negative response.

It is important to establish good rapport with your banker, with open lines of communication and feelings of mutual trust.

Please contact us for your copy of one of our other Business Advisory Publications, or download them free of charge from our website at www.kendons.co.nz.

You and Your Bankers

You and Your Business Plan

You and Your Business Acquisition

You and Your Business Records

You and Your Profitability

You and Your Qualifying Company

You and Your Review of Performance

You and Your Trust

You are Thinking About Going into Business

You and Your Wealth Creation

You and GST on Your Real Estate Transactions