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SME DIGEST

ADVICE FOR SMALL & MEDIUM SIZED ENTERPRISES

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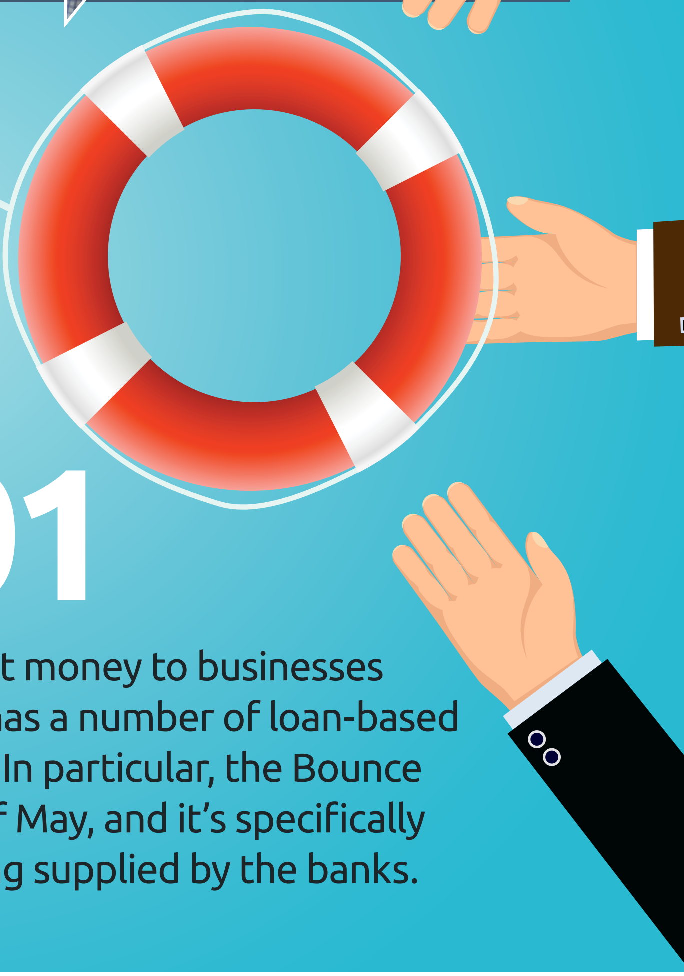
KEEPING AFLOAT

BOUNCE BACK LOANS 101



Just as the government has been handing out money to businesses under threat as a result of coronavirus, so it has a number of loan-based programmes to keep struggling firms afloat. In particular, the Bounce Back Loan (BBL) launched in the first week of May, and it's specifically aimed at the small business with monies being supplied by the banks.

By Adam Bernstein

BBLs have been very well received. According to data on smallbusiness.co.uk, the banks loaned £3.3bn on the first day with more than 100,000 businesses applying, with an average loan size of £30,000.

They're not going to be around forever; the book will close to new applications on 4 November.

Defining a Bounce Back Loan

Few think that debt is a good idea, after all, it means that another person or body has a hold over you and your business. However, for some, it is a form of funding that is actively courted – Apple is a big fan – which can provide working capital at very advantageous rates, especially in today's low interest world.

A BBL is a very specific thing in that it allows a business to borrow between £2,500 and £50,000 to a maximum 25% of its annual turnover over a six-year period. This compares very favourably to borrowing against a firm's reported profits (losses) after deducting expenses.

Now where a BBL comes into its own is that no interest is charged, and no repayments are made during the first year. For the remaining five years of the loan interest is fixed at 2.5% which is very low compared to a normal commercial loan; according to businessexpert.co.uk a commercial mortgage, for example, can cost between 2.25 and 18% plus arrangement fees. Credit card interest can be found sitting with interest rates in the mid-20s. And overdrafts are technically repayable on demand.

On top of the low cost is the ability to repay a loan early without being hit with any repayment charges. Further, there's no requirement or need to offer personal guarantees to secure the loan.

All of this follows from on the government backing the loans and covering interest and fees for the first year. And all that is needed to apply for a loan is, in theory, basic business data and proof the business has been affected by coronavirus and detail on what the money will be spent on.

The scheme is open to all - sole traders, (sole) directors of limited companies, and also those who are self-employed. But there is one snag - the business must have been going before March 2020, still running, and have been affected by coronavirus. Other criteria are that 50% of income must be from trading, it's not a business in difficulty as at 31 December 2019, it's not in a restricted sector, and it's not in receipt of another government lending programme. All of the details are on the gov.uk website, under *Apply for a coronavirus Bounce Back Loan*.

Seeking and obtaining a BBL doesn't remove the ability of the applicant to apply for the Self-Employment Income Support Scheme (SEISS) or Universal Credit. Also, unlike the furlough scheme, directors and employees can carry on working in the business. And as an added bonus, it's not taxable.

It's worth noting that applicants, once approved, cannot top up or increase a BBL. Nor can they apply for a second BBL for the same business. Thought must therefore be given to the amount requested.

A natural question to ask it what a BBL can be used for. As per the rules, there are few restrictions. All the regime says is that *"the business must confirm to the lender that the loan will only be used to provide an economic benefit to the business, for example providing working capital, and not for personal purposes."* This is so wide and can therefore include investment, the cost of running your business such as bills, debts and employees. Directors could also take money as dividends. Or the money can be used as a buffer against income shock.

The reality is that a BBL could be used to refinance expensive debt or even pay tax bills.

Where to apply

As to where to apply for a BBL, the government's website – gov.uk – lists all of the currently accredited banks. Search, again, for *Apply for a coronavirus Bounce Back Loan*. All the usual suspects are there - HSBC, Lloyds, TSB, Barclays, Santander, NatWest, RBS and Bank of Scotland, plus the Co-operative Bank, Clydesdale Bank, Yorkshire Bank, Danske Bank, Ulster Bank and Starling. Also, there's Starling, Paragon, Capitalontap, Arbuthnot, Coutts and Metro.

Noticeably missing is the Nationwide and Monzo.

Clearly those who already bank with these accredited institutions are going to find life much simpler as they're a known quantity. Those who want to get funding from these banks will have to open full (or feeder – 'basic') accounts if they don't already bank there and will have to counter the hurdles placed in their way such as anti-money laundering. It's also become apparent that the success of these loans had meant that many banks have closed to new applicants for the time being. The best bet might be to apply, if necessary, to a bank at which you're a personal customer.

Now here's the catch: While limited companies need a separate and distinct business account, sole traders don't. The problem is that BBLs generally require separate business accounts and this may lead to the need to have a fee-bearing account – only a handful including HSBC, Clydesdale Bank and Yorkshire Bank will lend to existing personal customers.

Fundamentally, the chances of success are improved by applying to your own bank or one where you have a personal account in good standing.

But beware that having an account with a bank doesn't guarantee success. As reported on a BBC Moneybox podcast at the end of June, Starling Bank in particular – it was the bank mainly discussed on the programme and so this situation probably applies to all – was found to be rejecting 16% of applicants. That said, 94% who were approved by Starling received the funds within 24 hours.

It's just as important that applicants set their expectations accordingly – with such a volume of applications it can take time to progress from a waiting list to being granted (rejected) for a loan. Partly, this is down to press of business but it's also down to due diligence checks to reduce fraud.

Lastly, if you are rejected by one bank there is nothing to prevent you applying to another, subject to the need to open a new account.

The downsides to consider

It's entirely true that a BBL is a very attractive proposition, and one that is backed by the government. Even so, a BBL is still debt which must be repaid, with interest, if it's kept for more than a year.

If you don't need the money and might be considered a spendthrift, then don't seek a BBL. It'll cause more trouble than it's worth.

And while the monies are backed by the government in case of non-repayment, if it's likely that the monies will just kick a problem further down the road then a BBL should also be avoided; while directors don't have to give a personal guarantee, a soft credit search at the minimum will be recorded.