

NEWTEK BUSINESS SERVICES INC

Form 10-Q

August 13, 2009

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## SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

### FORM 10-Q

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2009

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-16123

## NEWTEK BUSINESS SERVICES, INC.

(Exact name of registrant as specified in its charter)

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New York  
(State or other jurisdiction of  
incorporation or organization)

11-3504638  
(I.R.S. Employer  
Identification No.)

1440 Broadway, 17<sup>th</sup> floor, New York, NY  
(Address of principal executive offices)

10018  
(Zip Code)

Registrant's telephone number, including area code: (212) 356-9500

Indicate by checkmark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past ninety days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (Check one):

Large Accelerated Filer  Accelerated Filer   
Non-Accelerated Filer  Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of August 10, 2009, there were 37,038,324 of the Company's Common Shares issued and outstanding.

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**Table of Contents****Item 1. Financial Statements****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)****FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2009 AND 2008****(In Thousands, except for Per Share Data)**

	<b>Three Months ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Operating revenues	\$ 27,077	\$ 24,630	\$ 51,198	\$ 48,150
Operating expenses:				
Electronic payment processing costs	14,110	12,925	27,054	25,149
Salaries and benefits	4,497	5,985	9,307	12,564
Interest	3,605	2,194	6,122	4,483
Depreciation and amortization	1,570	1,766	3,219	3,576
Provision for loan losses	509	472	933	911
Other general and administrative costs	4,034	3,978	8,426	8,192
Total operating expenses	28,325	27,320	55,061	54,875
Operating loss before fair market value adjustment and benefit for income taxes	(1,248)	(2,690)	(3,863)	(6,725)
Net change in fair market value of credits in lieu of cash and notes payable in credits in lieu of cash	473	61	1,010	61
Loss before benefit for income taxes	(775)	(2,629)	(2,853)	(6,664)
Benefit for income taxes	131	524	1,145	1,762
Net loss	(644)	(2,105)	(1,708)	(4,902)
Net loss attributable to noncontrolling interests	7	123	95	226
Net loss attributable to Newtek Business Services, Inc.	\$ (637)	\$ (1,982)	\$ (1,613)	\$ (4,676)
Weighted average common shares outstanding basic and diluted	35,625	35,750	35,625	35,809
Loss per share basic and diluted	\$ (0.02)	\$ (0.06)	\$ (0.05)	\$ (0.13)

See accompanying notes to these unaudited condensed consolidated financial statements.

**Table of Contents****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS****JUNE 30, 2009 AND DECEMBER 31, 2008****(In Thousands, except for Per Share Data)**

	<b>June 30, 2009 Unaudited</b>	<b>December 31, 2008 (Note 1)</b>
<b><u>ASSETS</u></b>		
Cash and cash equivalents	\$ 18,594	\$ 16,852
Restricted cash	8,273	8,366
Credits in lieu of cash	49,640	70,559
SBA loans held for investment (net of reserve for loan losses of \$3,756 and \$3,420, respectively)	24,563	26,912
Accounts receivable (net of allowance of \$391 and \$192, respectively)	4,996	5,175
SBA loans held for sale		6,133
Prepaid expenses and other assets (net of accumulated amortization of deferred financing costs of \$2,335 and \$2,122, respectively)	8,901	9,998
Servicing asset (net of accumulated amortization and allowances of \$4,154 and \$3,756, respectively)	2,594	2,282
Fixed assets (net of accumulated depreciation and amortization of \$10,921 and \$9,477, respectively)	4,185	5,062
Intangible assets (net of accumulated amortization of \$13,413 and \$12,113, respectively)	5,042	6,096
Goodwill	12,092	12,092
<b>Total assets</b>	<b>\$ 138,880</b>	<b>\$ 169,527</b>
<b><u>LIABILITIES AND EQUITY</u></b>		
Liabilities:		
Accounts payable and accrued expenses	\$ 7,815	\$ 9,344
Notes payable	20,795	25,998
Deferred revenue	2,055	2,203
Notes payable in credits in lieu of cash	49,640	70,559
Deferred tax liability	4,147	5,344
<b>Total liabilities</b>	<b>84,452</b>	<b>113,448</b>
Commitments and contingencies		
Equity:		
Newtek Business Services, Inc. stockholders' equity:		
Preferred stock (par value \$0.02 per share; authorized 1,000 shares, no shares issued and outstanding)		
Common stock (par value \$0.02 per share; authorized 54,000 shares, issued and outstanding 36,657 and 36,667, respectively, not including 97 and 394 shares held in escrow, respectively)	733	733
Additional paid-in capital	58,294	58,232
Accumulated deficit	(6,158)	(4,545)
Treasury stock, at cost (1,026 shares)	(649)	(649)
<b>Total Newtek Business Services, Inc. stockholders' equity</b>	<b>52,220</b>	<b>53,771</b>
Noncontrolling interests	2,208	2,308
<b>Total equity</b>	<b>54,428</b>	<b>56,079</b>

Total liabilities and equity	\$ 138,880	\$ 169,527
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See accompanying notes to these unaudited condensed consolidated financial statements.

**Table of Contents****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)****FOR THE SIX MONTHS ENDED JUNE 30, 2009 AND 2008****(In Thousands)**

	<b>2009</b>	<b>2008</b>
Cash flows from operating activities:		
Net loss attributable to Newtek Business Services, Inc.	\$ (1,613)	\$ (4,676)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Income from tax credits	(4,250)	(2,954)
Accretion of interest expense	5,260	3,462
Fair market value adjustment	(1,010)	(61)
Deferred income taxes	(1,197)	(2,161)
Depreciation and amortization	3,219	3,576
Provision for loan losses	933	857
Gain on sale/recovery of investments in qualified business	(1,039)	
Net loss attributable to noncontrolling interests	(95)	(226)
Other, net	201	(30)
Changes in operating assets and liabilities:		
Originations of SBA loans held for sale	(2,669)	(10,977)
Proceeds from sale of SBA loans held for sale	8,802	9,818
Broker receivable	(1,249)	(5,646)
Prepaid expenses and other assets, accounts receivable and accrued interest receivable	1,541	(324)
Accounts payable, accrued expenses and deferred revenue	(1,674)	(1,802)
Other, net	(511)	262
Net cash provided by (used in) operating activities	4,649	(10,882)
Cash flows from investing activities:		
Investments in qualified businesses		(886)
Return of investments in qualified businesses	1,909	797
Purchase of fixed assets and customer merchant accounts	(899)	(2,018)
SBA loans originated for investment, net	(828)	(3,459)
Proceeds from sales of loans held for investment	400	
Payments received on SBA loans	1,862	2,333
Change in restricted cash	(107)	1,469
Net cash provided by (used in) investing activities	2,337	(1,764)

See accompanying notes to these unaudited condensed consolidated financial statements.

**Table of Contents****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)****FOR THE SIX MONTHS ENDED JUNE 30, 2009 AND 2008 (CONTINUED)**

	<b>2009</b>	<b>2008</b>
<b>Cash flows from financing activities:</b>		
Net repayment on notes payable	\$	\$ (338)
Purchase of treasury shares		(451)
Net (repayments) proceeds on bank notes payable	(5,203)	5,157
Other	(41)	(148)
Net cash (used in) provided by financing activities	(5,244)	4,220
Net increase (decrease) in cash and cash equivalents	1,742	(8,426)
Cash and cash equivalents beginning of period	16,852	25,372
Cash and cash equivalents end of period	\$ 18,594	\$ 16,946
<b>Supplemental disclosure of cash flow activities:</b>		
Reduction of credits in lieu of cash and notes payable in credits in lieu of cash balances due to delivery of tax credits to Certified Investors	\$ 19,079	\$ 10,136
Issuance of treasury shares for 401k match	\$	\$ 112
Reduction of structured insurance product and notes payable Certified Investors	\$	\$ 3,810

See accompanying notes to these unaudited condensed consolidated financial statements.



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**NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION:**

Newtek Business Services, Inc. ( Newtek ) is a holding company for several wholly- and majority-owned subsidiaries, including fourteen certified capital companies which are referred to as Capcos, and several portfolio companies in which the Capcos own non-controlling or minority interests. The Company provides a one-stop-shop for business services to the small- and medium-sized business market and uses state of the art web-based proprietary technology to be a low cost acquirer and provider of products and services. The Company partners with companies, credit unions, and associations to offer its services.

The Company's principal business segments are:

**Electronic Payment Processing:** Marketing, credit card processing and check approval services to the small- and medium-sized business market.

**Web Hosting:** CrystalTech Web Hosting, Inc., d/b/a/ Newtek Technology Services, ( NTS ) which offers shared and dedicated web hosting and related services to the small- and medium-sized business market.

**Small Business Finance:** Primarily consists of Newtek Small Business Finance, Inc. ( NSBF ), a nationally licensed, U.S. Small Business Administration ( SBA ) lender that originates, sells and services loans to qualifying small businesses, which are partially guaranteed by the SBA; and CDS Business Services, Inc. d/b/a Newtek Business Credit ( NBC ) which provides receivable financing.

**All Other:** Includes results from businesses formed from Investments in Qualified Businesses made through Capco programs which cannot be aggregated with other operating segments.

**Corporate Activities:** Corporate implements business strategy, directs marketing, provides technology oversight and guidance, coordinates and integrates activities of the segments, contracts with alliance partners, acquires customer opportunities, and owns our proprietary NewTracker referral system. Revenue and expenses not allocated to other segments, including interest income, Capco management fee income and corporate operations expenses.

**Capcos:** Fourteen certified capital companies which invest in small- and medium-sized businesses. They generate non-cash income from tax credits and non-cash interest and insurance expenses.

The condensed consolidated financial statements of Newtek Business Services, Inc., its Subsidiaries and FIN 46 consolidated entities (the Company or Newtek ) included herein have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America and include all wholly- and majority-owned subsidiaries, and several portfolio companies in which the Capcos own non-controlling minority interest in, or those which Newtek is considered to be the primary beneficiary of (as defined under FIN 46 and FIN 46R). All inter-company balances and transactions have been eliminated in consolidation. In accordance with the Company's fiscal 2009 adoption of SFAS No. 160, *Noncontrolling Interests in Consolidated Statements, an amendment of ARB No. 51* ( SFAS 160 ), noncontrolling interests (previously shown as minority interest) are reported below net loss under the heading Net loss attributable to noncontrolling interests in the unaudited condensed consolidated statements of operations and shown as a component of equity in the condensed consolidated balance sheets. See New Accounting Pronouncements for further discussion.

The accompanying notes to unaudited condensed consolidated financial statements should be read in conjunction with Newtek's 2008 Annual Report on Form 10-K. These financial statements have been prepared in accordance with instructions to Form 10-Q and Article 10 of Regulations S-X and, therefore, omit or condense certain footnotes and other information normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States. The results of operations for an interim period may not give a true indication of the results for the entire year. The December 31, 2008 consolidated balance sheet has been derived from the audited financial statements of that date, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

All financial information included in the tables in the following footnotes are stated in thousands, except per share data.

**NOTE 2 SIGNIFICANT ACCOUNTING POLICIES:**

*Use of Estimates*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and

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liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expense during the reporting period. The level of uncertainty in estimates and assumptions increases with the length of time until the underlying transactions are complete. The most significant estimates are with respect to valuation of investments in qualified businesses, asset impairment valuation, allowance for loan losses, valuation of servicing assets, chargeback reserves, tax valuation allowances and the fair value measurements used to value certain financial assets and financial liabilities. Actual results could differ from those estimates.

### ***Revenue Recognition***

The Company operates in several different segments. Revenues are recognized as services are rendered and are summarized as follows:

**Electronic payment processing revenue:** Electronic payment processing income is derived from the electronic processing of credit and debit card transactions that are authorized and captured through third-party networks. Typically, merchants are charged for these processing services on a percentage of the dollar amount of each transaction plus a flat fee per transaction. Certain merchant customers are charged miscellaneous fees, including fees for handling charge-backs or returns, monthly minimum fees, statement fees and fees for other miscellaneous services. In accordance with Emerging Issues Task Force ( EITF ) 99-19, Reporting Revenue Gross as a Principal versus Net as an Agent, revenues derived from the electronic processing of MasterCard® and Visa® sourced credit and debit card transactions are reported gross of amounts paid to sponsor banks.

The Company also derives revenues from acting as independent sales offices ( ISO ) for third-party processors ( residual revenue ) and from the sale of credit and debit card devices. Residual revenue is recognized monthly, based on contractual agreements with such processors to share in the residual income derived from the underlying merchant agreements. Revenues derived from sales of equipment are recognized at the time of shipment to the merchant.

**Web hosting revenue:** Web hosting revenues are primarily derived from monthly recurring service fees for the use of its web hosting and software support services. Customer set-up fees are billed upon service initiation and are recognized as revenue over the estimated customer relationship period of 2.5 years. Payment for web hosting and related services is generally received one month to three years in advance. Deferred revenues represent customer prepayments for upcoming web hosting and related services.

**Income from tax credits:** Following an application process, a state will notify a company that it has been certified as a Capco. The state then allocates an aggregate dollar amount of tax credits to the Capco. However, such amount is neither recognized as income nor otherwise recorded in the financial statements since it has yet to be earned by the Capco. The Capco is legally entitled to earn tax credits upon satisfying defined investment percentage thresholds within specified time requirements and corresponding non-recapture percentages. At June 30, 2009, the Company had Capcos in seven states and the District of Columbia. Each statute requires that the Capco invest a threshold percentage of Certified Capital in Qualified Businesses within the time frames specified. As the Capco meets these requirements, it avoids grounds under the statute for its disqualification for continued participation in the Capco program. Such a disqualification, or decertification as a Capco results in a recapture of all or a portion of the allocated tax credits; the proportion of the recapture is reduced over time as the Capco remains in general compliance with the program rules and meets the progressively increasing investment benchmarks.

As the Capco continues to make its investments in Qualified Businesses and, accordingly, places an increasing proportion of the tax credits beyond recapture, it earns an amount equal to the non-recapturable tax credits and records such amount as income from tax credits, with a corresponding asset called credits in lieu of cash, in the accompanying condensed consolidated balance sheets. The amount earned and recorded as income is determined by multiplying the total amount of tax credits allocated to the Capco by the percentage of tax credits immune from recapture (the earned income percentage) under the state statute. To the extent that the investment requirements are met ahead of schedule, and the percentage of non-recapturable tax credits is accelerated, the present value of the tax credit earned is recognized currently and the asset, credits in lieu of cash, is accreted up to the amount of tax credits available to the Certified Investors. If the tax credits are earned before the state is required to make delivery (i.e., investment requirements are met ahead of schedule, but credits can only be used by the certified investor in a future year), then the present value of the tax credits earned are recorded upon completion of the requirements, in accordance with Accounting Principles Board Opinion No. 21. The receivable is calculated at fair value; see note 3 for a full discussion. Delivery of the tax credits to the Certified Investors results in a decrease of the receivable and the notes payable in credits in lieu of cash.

The allocation and utilization of Capco tax credits is controlled by the state law. In general, the Capco applies for tax credits from the state and is allocated a specific dollar amount of credits which are available to be earned. The Capco provides the state with a list of the Certified Investors, who have contractually agreed to accept the tax credits in lieu of cash interest payments on their notes. The tax credits are claimed by the Certified Investors on their state premium tax return as provided under each state



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Capco and tax law. State regulations specify the amount of tax credits a Certified Investor can claim and the period in which they can claim them. Each state periodically reviews the Capco's operations to verify the amount of tax credits earned. In addition, the state maintains a list of Certified Investors and therefore has the ability to determine whether the Certified Investor is allowed to claim this deduction.

**Sales and Servicing of SBA Loans:** NSBF originates loans to customers under the SBA program that generally provides for SBA guarantees of 50% to 90% of each loan, subject to a maximum guarantee amount. NSBF sells the guaranteed portion of each loan to a third party and retains the unguaranteed principal portion in its own portfolio. A gain is recognized on the guaranteed portions of these loans through collection on sale of a premium over the adjusted carrying value or a par sale with excess servicing. Commencing on January 1, 2008, the Company began to recognize the gain on sale of the guaranteed portion of the loans on the trade date rather than the date of settlement, under the terms of SFAS No. 156 Accounting for Servicing of Financial Assets an amendment of FASB Statement No. 140 for 2009 and 2008.

In each loan sale, the Company retains servicing responsibilities and receives servicing fees of a minimum of 1% of the guaranteed loan portion sold. The Company is required to estimate its adequate servicing compensation in the calculation of its servicing asset. The purchasers of the loans sold have no recourse to the Company for failure of customers to pay amounts contractually due.

In accordance with SFAS 156, upon sale of the loans to third parties, NSBF separately recognizes at fair value any servicing assets or servicing liabilities first, and then allocates the previous carrying amount between the assets sold and the interests that continue to be held by the transferor (the unguaranteed portion of the loan) based on their relative fair values at the date of transfer. The difference between the proceeds received and the allocated carrying value of the financial assets sold is recognized as a gain on sale of loans.

In accordance with SFAS 140, upon sale of the loans to third parties, the Company's investment in an SBA loan is allocated among the retained portion of the loan (unguaranteed), the sold portion of the loan (guaranteed) and the value of loan servicing retained, based on the relative estimated fair market values of each component at the sale date. The difference between the proceeds received and the allocated carrying value of the loan sold is recognized as a gain on sale of loans.

Each class of servicing assets and liabilities are subsequently measured under SFAS 156 using either the amortization method or the fair value measurement method. The amortization method, which NSBF has chosen to continue applying to its servicing asset, amortizes the asset in proportion to, and over the period of, the estimated future net servicing income on the underlying sold portion of the loans (guaranteed) and assesses the servicing asset for impairment based on fair value at each reporting date. In the event future prepayments are significant or impairments are incurred and future expected cash flows are inadequate to cover the unamortized servicing assets, additional amortization or impairment charges would be recognized. The Company uses an independent valuation specialist to estimate the fair value of the servicing asset.

In evaluating and measuring impairment of servicing assets, NSBF stratifies its servicing assets based on year of loan and loan term which are key risk characteristics of the underlying loan pools. The fair value of servicing assets is determined by calculating the present value of estimated future net servicing cash flows, using assumptions of prepayments, defaults, servicing costs and discount rates that NSBF believes market participants would use for similar assets.

If NSBF determines that the impairment for a stratum is temporary, a valuation allowance is recognized through a charge to current earnings for the amount the amortized balance exceeds the current fair value. If the fair value of the stratum were to later increase, the valuation allowance may be reduced as a recovery. However, if NSBF determines that an impairment for a stratum is other than temporary, the value of the servicing asset and any related valuation allowance is written-down.

**Interest and Small Business Administration ( SBA ) Loan Fees SBA Loans:** Interest income on loans is recognized as earned. Loans are placed on non-accrual status if they are 90 days past due with respect to principal or interest and, in the opinion of management, interest or principal on individual loans is not collectible, or at such earlier time as management determines that the collectability of such principal or interest is unlikely. Such loans are designated as impaired non-accrual loans. All other loans are defined as performing loans. When a loan is designated as non-accrual, the accrual of interest is discontinued, and any accrued but uncollected interest income is reversed and charged against current operations. While a loan is classified as non-accrual and the future collectability of the recorded loan balance is doubtful, collections of interest and principal are generally applied as a reduction to principal outstanding.

The Company passes certain expenditures it incurs to the borrower, such as forced placed insurance, insufficient funds fees, or fees it assesses, such as late fees, with respect to managing the loan. These expenditures are recorded when incurred. Due to the uncertainty with respect to collection of these passed through expenditures or assessed fees, any funds received to reimburse the Company are recorded on a cash basis as other income.



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**Insurance commissions:** Revenues are comprised of commissions earned on premiums paid for insurance policies and are recognized at the time the commission is earned. At that date, the earnings process has been completed and the Company can estimate the impact of policy cancellations for refunds and establish reserves. The reserve for policy cancellations is based on historical cancellation experience adjusted by known circumstances.

**Other income:** Other income represents revenues generated by NBC, as well as revenues derived from operating units that cannot be aggregated with other business segments, and one-time recoveries or gains on qualified investments. Revenue is recorded when there is pervasive evidence of an agreement, the related fees are fixed, the service, and or product has been delivered, and the collection of the related receivable is assured. Other income for the three and six months ended June 30, 2009 includes a \$1,000,000 recovery of a qualified investment previously written off. Other income particular to NBC include the following components:

**Receivable fees:** Receivable fees are derived from the funding (purchase) of receivables from finance clients. The percentage of fees is set when entered into an agreement with the client. The Company recognizes the revenue on the date the receivable is purchased. The Company does not take ownership of the receivables until funds are released which then constitutes a purchase of a client's asset. The Company also has arrangements with certain of its clients whereby it purchases the client's receivables and charges interest at a specified rate based on the amount of funds advanced against such receivables. The interest income is recognized as earned.

**Late fees:** Late fees are derived from receivables the Company has already purchased that have gone over a certain period (usually over 30 days) without payment. The client or the client's customer is charged a late fee according to the agreement with the client.

**Billing fees:** Billing fees are derived from billing-only (non-finance) clients. These fees are recorded when earned, which occurs when the service is rendered.

**Other fees:** These fees include annual fees, due diligence fees, termination fees, under minimum fees and other fees including, finance charges, supplies sold to clients, NSF fees, wire fees and administration fees. These fees are charged upon funding, takeovers or liquidation of finance clients. Finally, the Company also receives commission revenue from various sources.

The detail of total operating revenues included in the condensed consolidated statements of operations is as follows for the three and six months ended:

(In thousands):	Three months ended		Six months ended	
	June 30:	June 30:	June 30:	June 30:
	2009	2008	2009	2008
Electronic payment processing	\$ 16,881	\$ 15,921	\$ 32,641	\$ 31,104
Web hosting	4,702	4,499	9,374	8,775
Interest income	430	831	928	1,804
Income from tax credits	2,714	1,491	4,250	2,954
Premium on loan sales	137	326	582	476
Servicing fee	424	437	825	922
Insurance commissions	217	350	417	593
Other income	1,572	775	2,181	1,522
Totals	\$ 27,077	\$ 24,630	\$ 51,198	\$ 48,150

**Electronic Payment Processing Costs**

Electronic payment processing costs consist principally of costs directly related to the processing of merchant sales volume, including interchange fees, VISA and MasterCard dues and assessments, bank processing fees and costs paid to third-party processing networks. Such costs are recognized at the time the merchant transactions are processed or when the services are performed. Two of the most significant

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components of electronic processing expenses include interchange and assessment costs, which are set by the credit card associations. Interchange costs are passed on to the entity issuing the credit card used in the transaction and assessment costs are retained by the credit card associations. Interchange and assessment fees are billed primarily as a percent of dollar volume processed and, to a lesser extent, as a per transaction fee. In addition to costs directly related to the processing of merchant sales volume, electronic payment processing costs also include residual expenses. Residual expenses represent fees paid to third-party sales referral sources. Residual expenses are paid under various formulae as contracted with such third-party referral sources, but are generally linked to revenues derived from merchants successfully referred to the Company and that begin using the Company for merchant processing services. Such residual expenses are typically ongoing as long as the referred merchant remains a customer of the Company and are recognized as expenses as related revenues are recognized in the Company's condensed consolidated statements of operations.



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Restricted cash includes cash collateral relating to a letter of credit; monies due on loan-related remittances and insurance premiums received by the Company and due to third parties; cash held by the Capcos restricted for use in managing and operating the Capco, making qualified investments and for the payment of income taxes; and a cash account maintained as a reserve against chargeback losses.

***Purchased Receivables***

Purchased receivables are recorded at the point in time when cash is released to the seller. A majority of the receivables purchased have recourse and are charged back to the seller if aged over 60, 90 or 120 days, depending on contractual agreements. Purchased receivables are included in accounts receivable on the condensed consolidated balance sheet.

***Investments in Qualified Businesses***

The various interests that the Company acquires in its qualified investments are accounted for under three methods: consolidation, equity method and cost method. The applicable accounting method is generally determined based on the Company's voting interest or the economics of the transaction if the investee is determined to be a variable interest entity.

*Consolidation Method.* Investments in which the Company directly or indirectly owns more than 50% of the outstanding voting securities, those the Company has effective control over, or those deemed to be a variable interest entity in which the Company is the primary beneficiary under the provisions of FIN 46R ( FIN 46 consolidated entity ) are generally accounted for under the consolidation method of accounting. Under this method, an investment's financial position and results of operations are reflected within the Company's condensed consolidated financial statements. All significant inter-company accounts and transactions are eliminated, including returns of principal, dividends, interest received and investment redemptions. The results of operations and cash flows of a consolidated operating entity are included through the latest interim period in which the Company owned a greater than 50% direct or indirect voting interest, exercised control over the entity for the entire interim period or was otherwise designated as the primary beneficiary. Upon dilution of control below 50%, or upon occurrence of a triggering event requiring reconsideration as to the primary beneficiary of a variable interest entity, the accounting method is adjusted to the equity or cost method of accounting, as appropriate, for subsequent periods.

*Equity Method.* Investees that are not consolidated, but over which the Company exercises significant influence, are accounted for under the equity method of accounting. Whether or not the Company exercises significant influence with respect to an investee depends on an evaluation of several factors including, among others, representation on the investee's Board of Directors and ownership level, which is generally a 20% to 50% interest in the voting securities of the investee, including voting rights associated with the Company's holdings in common, preferred and other convertible instruments in the investee. Under the equity method of accounting, an investee's accounts are not reflected within the Company's condensed consolidated financial statements; however, the Company's share of the earnings or losses of the investee is reflected in the Company's condensed consolidated financial statements.

*Cost Method.* Investees not accounted for under the consolidation or the equity method of accounting are accounted for under the cost method of accounting. Under this method, the Company's share of the net earnings or losses of such companies is not included in the Company's condensed consolidated financial statements. However, cost method impairment charges are recognized, as necessary, in the Company's condensed consolidated financial statements. If circumstances suggest that the value of the investee has subsequently recovered, such recovery is not recorded until ultimately liquidated or realized.

The Company's debt and equity investments have substantially been made with funds available to Newtek through the Capco programs. These programs generally require that each Capco meet a minimum investment benchmark within five years of initial funding. In addition, any funds received by a Capco as a result of a debt repayment or equity return may, under the terms of the Capco programs, be reinvested and counted towards the Capcos' minimum investment benchmarks.

***Stock-Based Compensation***

The Company applies SFAS 123 (revised 2004), Share-Based Payment ( SFAS 123R ). SFAS 123R requires all share-based payments to employees to be recognized in the financial statements based on their fair values using an option-pricing model at the date of grant.

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As of June 30, 2009 and 2008 the Company had two share-based compensation plans. For the three and six months ended June 30, 2009 and 2008, compensation cost charged to operations for those plans was \$28,000 and \$65,000 in 2009, respectively, and \$26,000 and \$148,000 in 2008, respectively, and is included in salaries and benefits in the accompanying condensed consolidated statements of operations.

There were no options or restricted stock awards granted during the six months ended June 30, 2009.

In March 2008, Newtek granted its six independent directors an aggregate of 197,434 options valued at \$87,000. Option awards are granted with an exercise price equal to the market price of the Company's stock at the date of grant. The options vest immediately and expire 10 years from the date of grant. The fair value of each option award is estimated on the date of grant using a Black-Scholes option valuation model that uses the following assumptions: 5 year expected life, risk-free interest rate of 2.51% and expected volatility of the Company's stock of 53.48%. Expected volatilities are based on the historical volatility of the Company's stock and other factors. The risk-free rate for periods during the expected life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Expected term was determined using the simplified method under Staff Accounting Bulletin No. 107, Valuation of Share-Based Payment Arrangements for Public Companies

As of June 30, 2009 and December 31, 2008, there was \$133,000 and \$238,000 of total unrecognized compensation costs related to non-vested share-based compensation arrangements granted under the Plans, respectively. That cost is expected to be recognized ratably through the month ending July 31, 2010.

### ***Fair Value***

Effective January 1, 2008, the Company determines the fair market values of its financial instruments based on the fair value hierarchy established in SFAS No. 157 Fair Value Measurements ( SFAS 157 ) which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value which are provided below. The Company carries its credits in lieu of cash, prepaid insurance and notes payable in credits in lieu of cash at fair value in accordance with SFAS No. 159 The Fair Value Option for Financial Assets and Financial Liabilities ( SFAS 159 ). The Company also carries impaired loans and other real estate owned at fair value.

- Level 1** Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities and derivative contracts that are traded in an active exchange market, as well as certain U.S. Treasury, other U.S. Government and agency mortgage-backed debt securities that are highly liquid and are actively traded in over-the-counter markets.
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted prices that are traded less frequently than exchange-traded instruments and derivative contracts whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. This category generally includes certain U.S. Government and agency mortgage-backed debt securities, corporate debt securities, derivative contracts and residential mortgage loans held-for-sale.
- Level 3** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category generally includes certain private equity investments, retained residual interests in securitizations, residential mortgage servicing rights, and highly structured or long-term derivative contracts.

### ***Income Taxes***

Deferred tax assets and liabilities are computed based upon the differences between the financial statement and income tax basis of assets and liabilities using the enacted tax rates in effect for the year in which those temporary differences are expected to be realized or settled. If available evidence suggests that it is more likely than not that some portion or all of the deferred tax assets will not be realized, a valuation allowance is required to reduce the deferred tax assets to the amount that is more likely than not to be realized.

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***Accounting for Uncertainty in Income Taxes***

The FASB issued Interpretation No. 48 ( FIN-48 ), Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109. FIN-48 recognizes that the ultimate deductibility of positions taken or expected to be taken on tax returns is often uncertain. It provides guidance on when tax positions claimed by an entity can be recognized (*recognition*) and guidance on the dollar amount at which those positions are recorded (*measurement*). In order to recognize the benefits associated with a tax position taken (i.e., generally a deduction on a corporation's tax return), the entity must conclude that the ultimate allowability of the deduction is more likely than not. If the ultimate allowability of the tax position exceeds 50% (i.e., it is more likely than not), the benefit associated with the position is recognized at the largest dollar amount that has more than a 50% likelihood of being realized upon ultimate settlement. Differences between tax positions taken in a tax return and recognized in accordance with FIN-48 will generally result in (1) an increase in income taxes currently payable or a reduction in an income tax refund receivable or (2) an increase in a deferred tax liability or a decrease in a deferred tax asset, or both (1) and (2).

FIN-48 also provides guidance on:

Derecognizing the benefits associated with a recognized tax position where subsequent events indicate that it is *not* more likely than not that the entity will benefit from the tax position taken

Classification of financial statement elements that result from recognizing benefits associated with uncertain tax positions

Treatment of interest and penalties related to uncertain tax positions

Accounting for uncertain tax positions in interim periods

Disclosure and transition

***Concentration of Credit Risk***

Financial instruments that potentially subject the Company to a concentration of credit risk consist of cash, cash equivalents and accounts receivable. The Company maintains its cash and cash equivalents with major financial institutions and at times, cash balances with any one financial institution may exceed Federal Deposit Insurance Corporation (FDIC) insured limits.

For the six months ended June 30, 2009 and 2008, no single customer accounted for 10% or more of the Company's revenue or of total accounts receivable.

***Fair Value of Financial Instruments***

SFAS No. 107, Disclosures about Fair Value of Financial Instruments ( SFAS 107 ), requires the disclosure of the estimated fair values of financial instruments. Excluding property and equipment, substantially all of the Company's assets and liabilities are considered financial instruments as defined by SFAS 107. Fair value estimates are subjective in nature and are dependent on a number of significant assumptions associated with each instrument or group of similar instruments, including estimates of discount rates, risks associated with specific financial instruments, estimates of future cash flows and relevant available market information.

The methods and assumptions used to estimate fair values are set forth in the following paragraphs for each major grouping of the Company's financial instruments.

The carrying values of the following balance sheet items approximate their fair values primarily due to their liquidity and short-term or adjustable-yield nature:

Cash and cash equivalents

Bank notes payable

Accrued interest receivable and payable

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The carrying values of accounts payable and accrued expenses approximate fair value because of the short-term maturity of these instruments. The carrying value of investments in qualified businesses, loans receivable, and notes payable approximate fair value based on management's estimates.

***New Accounting Pronouncements***

In February 2008, the FASB issued FSP No. FAS 157-2, *Effective Date for FASB Statement No. 157* ( FSP FAS 157-2 ). This FSP permits the delayed application of SFAS 157 for nonfinancial assets and nonfinancial liabilities, as defined in this FSP, except for those that are recognized or disclosed at fair value in the financial statements at least annually, until the beginning of the Company's fiscal 2009. Effective January 1, 2009, the Company fully adopted the provision of SFAS 157 by adopting the provisions relating to its nonfinancial assets and liabilities. The Company adopted the provisions relating to financial assets and liabilities in the prior year and its adoption of SFAS 157 relating to nonfinancial assets and liabilities did not have a material impact on its financial position or results of operations.

In September 2008, the FASB ratified EITF Issue No. 08-5, *Issuer's Accounting for Liabilities Measured at Fair Value With a Third-Party Credit Enhancement* ( EITF 08-5 ). EITF 08-5 provides guidance for measuring liabilities issued with an attached third-party credit enhancement (such as a guarantee). It clarifies that the issuer of a liability with a third-party credit enhancement (such as a guarantee) should not include the effect of the credit enhancement in the fair value measurement of the liability. EITF 08-5 is effective for the first reporting period beginning after December 15, 2008. The Company concluded that EITF 08-5 does not impact its condensed consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (R), *Business Combinations* ( SFAS 141(R) ). SFAS 141(R) requires an acquirer to measure the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at their fair values on the acquisition date, with goodwill being the excess value over the net identifiable assets acquired. SFAS 141(R) is effective for financial statements issued for fiscal years beginning after December 15, 2008. The Company has adopted SFAS 141(R) and there was no material impact to the condensed consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements* an amendment of Accounting Research Bulletin No. 51 ( SFAS 160 ). SFAS 160 addresses the accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income or loss attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest, and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. SFAS 160 also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. SFAS 160 is effective for fiscal years beginning after December 15, 2008. The Company adopted the provisions of SFAS 160 in the first quarter of 2009. As a result of the adoption, the Company has reported noncontrolling interests as a component of equity in the condensed consolidated balance sheets and the net loss attributable to noncontrolling interests has been separately identified in the unaudited condensed consolidated statements of operations. The prior periods presented have also been retrospectively restated to conform to the current classification required by SFAS 160. Other than the change in presentation of noncontrolling interests, the adoption of SFAS 160 had no impact on the condensed consolidated financial statements.

In April 2009, the FASB issued FSP No. FAS 107-1 and APB 28-1 which amended both SFAS No. 107 and APB Opinion No. 28 to require that disclosures concerning the fair value of financial instruments be presented in interim as well as in annual financial statements. In addition, the FASB issued FSP No. FAS 157-4 which amended SFAS No. 157 to provide additional guidance for determining the fair value of a financial asset or financial liability when the volume and level of activity for such asset or liability have decreased significantly. FSP No. FAS 157-4 also provided guidance for determining whether a transaction is an orderly one. The FASB also issued FSP No. FAS 115-2 and FAS 124-2 which revised and expanded the guidance concerning the recognition and measurement of other-than-temporary impairments of debt securities classified as available for sale or held to maturity. In addition, it required enhanced disclosures concerning such impairment for both debt and equity securities. The requirements of these FSPs are effective for interim reporting periods ending after June 15, 2009. Early adoption is permitted for interim periods ending after March 15, 2009, but only if the election is made to adopt all the FSPs. Disclosures for earlier periods presented for comparative purposes at initial adoption are not required. In periods after initial adoption, comparative disclosures are required only for periods ending after initial adoption. The Company has adopted the FSPs for the second quarter of 2009.

In May 2009, the FASB issued SFAS No. 165, *Subsequent Events* ( FAS 165 ), which provides guidance to establish general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. FAS 165 requires entities to disclose the date through which subsequent

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events were evaluated as well as the rationale for why that date was selected. FAS 165 is effective for interim and annual periods ending after June 15, 2009 and, accordingly, the Company adopted FAS 165 during the second quarter of 2009. FAS 165 requires public entities evaluate subsequent events through the date that the financial statements are issued. The Company has evaluated subsequent events through the time of filing these condensed consolidated financial statements with the Securities and Exchange Commission ( SEC ) on August 13, 2009.

In June 2009, the FASB issued SFAS No. 166, Accounting for Transfers of Financial Assets an amendment of FASB Statement No. 140 ( FAS 166 ), which requires entities to provide more information regarding sales of securitized financial assets and similar transactions, particularly if the entity has continuing exposure to the risks related to transferred financial assets. FAS 166 eliminates the concept of a qualifying special-purpose entity, changes the requirements for derecognizing financial assets and requires additional disclosures. FAS 166 is effective for fiscal years beginning after November 15, 2009. The Company is currently evaluating the impact of adopting FAS 166 on its condensed consolidated financial statements.

In June 2009, the FASB issued SFAS No. 167, Amendments to FASB Interpretation No. 46(R) ( FAS 167 ), which modifies how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. FAS 167 clarifies that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity s purpose and design and a company s ability to direct the activities of the entity that most significantly impact the entity s economic performance. FAS 167 requires an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity and additional disclosures about a company s involvement in variable interest entities and any significant changes in risk exposure due to that involvement. FAS 167 is effective for fiscal years beginning after November 15, 2009. The Company is currently evaluating the impact of adopting FAS 167 on its condensed consolidated financial statements.

In June 2009, the FASB issued SFAS No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162 ( FAS 168 ). FAS 168 establishes the FASB Accounting Standards Codification (the Codification ) as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. GAAP. The Codification does not change current U.S. GAAP, but is intended to simplify user access to all authoritative U.S. GAAP by providing all the authoritative literature related to a particular topic in one place. The Codification is effective for interim and annual periods ending after September 15, 2009 and, as of the effective date, all existing accounting standard documents will be superseded. The Codification is effective for the Company in the third quarter of 2009 and, accordingly, the Quarterly Report on Form 10-Q for the quarter ending September 30, 2009 and all subsequent public filings will reference the Codification as the sole source of authoritative literature.

**NOTE 3 FAIR VALUE MEASUREMENTS:**

**FAIR VALUE OPTION ELECTIONS**

Effective January 1, 2008, the Company adopted SFAS No. 157 Fair Value Measurements ( SFAS 157 ), concurrent with its adoption of SFAS No. 159 The Fair Value Option for Financial Assets and Financial Liabilities ( SFAS 159 ). SFAS 157 clarifies the definition of fair value and describes methods available to appropriately measure fair value in accordance with GAAP. SFAS 157 applies whenever other accounting pronouncements require or permit fair value measurements. SFAS 159 allows entities to irrevocably elect fair value as the initial and subsequent measurement attribute for certain financial assets and financial liabilities that are not otherwise required to be measured at fair value, with changes in fair value recognized in earnings as they occur. SFAS 159 establishes presentation and disclosure requirements designed to improve comparability between entities that elect different measurement attributes for similar assets and liabilities. The Company adopted SFAS 159 effective January 1, 2008 concurrent with the adoption of SFAS 157 for valuing its Capcos credits in lieu of cash, notes payable in credits in lieu of cash and prepaid insurance.

The Company adopted SFAS 159 in order to reflect in its financial statements the assumptions that market participants use in evaluating these financial instruments. Under the cost basis of accounting, the discount rates used to calculate the present value of the credits in lieu of cash and notes payable in credits in lieu of cash did not reflect the credit enhancements that the Company s Capcos obtained from AIG, namely its AA+ rating at such time, for their debt issued to certified investors. Instead the cost paid for the credit enhancements was recorded as prepaid insurance and amortized on a straight-line basis over the term of the credit enhancements.

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With the adoption of SFAS 159 and the concurrent adoption of SFAS 157, credits in lieu of cash and notes payable in credits in lieu of cash are valued based on the yields at which financial instruments would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell, both parties having reasonable knowledge of relevant facts. SFAS 157 requires the fair value of the assets or liabilities to be determined based on the assumptions that market participants use in pricing the financial instrument. In developing those assumptions, the Company identified characteristics that distinguish market participants generally, and considered factors specific to (a) the asset type, (b) the principal (or most advantageous) market for the asset group, and (c) market participants with whom the reporting entity would transact in that market.

Based on the aforementioned characteristics and in view of the AIG credit enhancements, the Company believes that market participants purchasing or selling its Capcos debt, and therefore its credits in lieu of cash, and notes payable in credits in lieu of cash view nonperformance risk to be equal to the risk of an AIG nonperformance risk and as such both the fair value of credits in lieu of cash and notes payable in credits in lieu of cash should be priced to yield a rate equal to an applicable AIG U.S. Dollar denominated debt instrument. Because the value of notes payable in credits in lieu of cash directly reflects the credit enhancement obtained from AIG, the unamortized cost relating to the credit enhancement will cease to be separately carried as an asset on Company's condensed consolidated balance sheet and is incorporated in notes payable in credits in lieu of cash.

**Assets and Liabilities Measured at Fair Value on a Recurring Basis are as follows (in thousands):**

	Fair Value Measurements Using:			
	Total	Level 1	Level 2	Level 3
<b>Assets:</b>				
Credits in lieu of cash	\$ 49,640	\$	\$ 49,640	\$
<b>Prepaid insurance</b>				
Total assets	\$ 49,640	\$	\$ 49,640	\$
<b>Liabilities:</b>				
Notes payable in credits in lieu of cash	\$ 49,640	\$	\$ 49,640	\$

**Credits in lieu of cash and Notes payable in credits in lieu of cash**

The Company elected to account for both credits in lieu of cash and notes payable in credits in lieu of cash at fair value in accordance with SFAS 159 in order to reflect in its condensed consolidated financial statements the assumptions that market participants use in evaluating these financial instruments.

**Prepaid insurance**

The Company has determined that the effect of the credit enhancement obtained from AIG is inseparable from the notes payable in credits in lieu of cash. In adopting SFAS 159 the prepaid insurance unamortized cost relating to the credit enhancement ceased to be separately carried as an asset on the Company's condensed consolidated balance sheet and is incorporated in notes payable in credits in lieu of cash.

The Company's Capcos debt, enhanced by AIG insurance, effectively bears the nonperformance risk of AIG. Therefore the Company calculates the fair value of both the Credits in lieu of cash and Notes payable in credits in lieu of cash using the yields of various AIG notes with similar maturities to each of the Company's respective Capcos debt. The Company elected to discontinue utilizing AIG's 7.70% Series A-5 Junior Subordinated Debentures (the AIG Debentures) because those long maturity debentures began to trade with characteristics of a preferred stock after AIG received financing from the United States Government. The Company considers the AIG Note Basket a Level 2 input under SFAS 157, since it is a quoted yield for a similar liability that is traded in an active exchange market. The Company selected these AIG Note Baskets as the most representative of the nonperformance risk associated with the CAPCO notes because they are AIG issued notes, are actively traded and because maturities match Credits in lieu of cash and Notes payable in credits in lieu of cash.





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After calculating the fair value of both the Credits in lieu of cash and Notes payable in credits in lieu of cash, the Company compares their values. This calculation is done on a quarterly basis. Calculation differences primarily due to tax credit receipt versus delivery timing may cause the value of the Credits in lieu of cash to differ from that of the Notes payable in credits in lieu of cash. Because the Credits in lieu of cash asset has the single purpose of paying the Notes payable in credits in lieu of cash and has no other value to the Company, Newtek determined that the Credits in lieu of cash should equal the Notes payable in credits in lieu of cash.

As of March 31, 2009, the present value of the credits in lieu of cash was \$46,866,000 and notes payable in credits in lieu of cash was \$46,260,000. On that date, the yield on the AIG Note Basket was 27.56%. As of June 30, 2009, the date the Company revalued the asset and liability, the yields on the AIG notes averaged 18.27% reflecting changes in interest rates in the marketplace. This decrease in yield increased both the fair value of the credits in lieu of cash by \$6,157,000 to \$49,388,000 from an expected value of \$43,231,000 assuming the yield had remained unchanged from March 31, 2009, and the fair value of the notes payable in credits in lieu of cash by \$6,539,000 to \$49,640,000 from an expected value of \$43,101,000 assuming the yield had remained unchanged from March 31, 2009. The Company increased the value of the credits in lieu of cash to equal the value of the notes payable in credits in lieu of cash because the credits in lieu of cash can only be used to satisfy the liability and must equal the value of the notes payable in credits in lieu of cash at all times. The net change in fair value reported in the Company's condensed consolidated statement of operations for the three and six month periods ended June 30, 2009 was a gain of \$473,000 and \$1,010,000, respectively.

Changes in the future yield of the AIG issued debt selected for valuation purposes will result in changes to the fair values of the credits in lieu of cash and notes payable in credits in lieu of cash when calculated for future periods; these changes will be reported through the Company's condensed consolidated statements of operations.

**OTHER FAIR VALUE MEASUREMENTS**

**Assets and Liabilities Measured at Fair Value on a Non-recurring Basis are as follows (in thousands):**

	Fair Value Measurements at Reporting Date Using:			
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Impaired loans	\$ 7,126	\$	\$	\$ 7,126
Other real-estate owned	456		456	
<b>Total assets</b>	\$ 7,582	\$	\$ 456	\$ 7,126

**Impaired loans**

Impairment of a loan within the scope of SFAS 114 is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or the fair value of the collateral if the loan is collateral dependent. Impaired loans for which the carrying amount is based on fair value of the underlying collateral are included in assets and reported at estimated fair value on a non-recurring basis, both at initial recognition of impairment and on an on-going basis until recovery or charge-off of the loan amount. The determination of impairment involves management's judgment in the use of market data and third party estimates regarding collateral values. Valuations in the level of impaired loans and corresponding impairment as defined under SFAS 114 affect the level of the reserve for loan losses.

**Servicing asset**

The estimated fair value of servicing assets is calculated on an annual basis by several methods, one of which is by an independent third party using an estimated cash flow model with observable inputs that affect the price of an asset/liability. This is considered a Level 3 valuation by the Company.

**Table of Contents****Other real-estate owned (included in Prepaid expenses and other assets)**

The estimated fair value of other real-estate owned is calculated using observable market information, including bids from prospective purchasers and pricing from similar market transactions where available. The value is generally discounted between 20-25% based on market valuations as well as expenses associated with securing our interests. Where bid information is not available for a specific property, the valuation is principally based upon recent transaction prices for similar properties that have been sold. These comparable properties share comparable demographic characteristics. Other real estate owned is generally classified within Level 2 of the valuation hierarchy.

**NOTE 4 SBA LOANS:**

SBA loans are primarily concentrated in the hotel and motel industry (11% of the portfolio) and the restaurant industry (13% of the portfolio), as well as geographically in Florida (28% of the portfolio) and New York (16% of the portfolio). Below is a summary of the activity in the SBA loans held for investment, net of SBA loan loss reserves for the six months ended June 30, 2009 (In thousands):

Balance at December 31, 2008	\$ 26,912
SBA loans funded for investment	912
Payments received	(1,862)
SBA loans held for investment, sold	(400)
Provision for SBA loan losses	(933)
Loans foreclosed into real estate owned	(66)
<b>Balance at June 30, 2009</b>	<b>\$ 24,563</b>

Below is a summary of the activity in the reserve for loan losses for the six months ended June 30, 2009 (In thousands):

Balance at December 31, 2008	\$ 3,420
SBA loan loss provision	933
Recoveries	21
Loan charge-offs	(618)
<b>Balance at June 30, 2009</b>	<b>\$ 3,756</b>

Below is a summary of the activity in the SBA loans held for sale for the six months ended June 30, 2009 (In thousands):

Balance at December 31, 2008	\$ 6,133
Loan originations for sale	2,669
Loans sold	(8,802)
<b>Balance at June 30, 2009</b>	<b>\$</b>

All loans are priced at the Prime interest rate plus approximately 2.75% to 3.75%. The only loans with a fixed interest rate are defaulted loans of which the guaranteed portion sold is repurchased from the secondary market by the SBA, while the unguaranteed portion of the loans still remains with the Company. As of June 30, 2009 and December 31, 2008, net SBA loans receivable held for investment with adjustable interest rates amounted to \$24,160,000 and \$25,948,000, respectively.

For the six months ended June 30, 2009 and 2008, the Company funded approximately \$3,581,000 and \$14,518,000 in loans and sold approximately \$8,802,000 and \$9,818,000 of the guaranteed portion of the loans, respectively.

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The outstanding balances of loans past due ninety days or more and still accruing interest as of June 30, 2009 and December 31, 2008 amounted to \$591,000 and \$626,000, respectively.

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At June 30, 2009 and December 31, 2008, total impaired non-accrual loans amounted to \$7,126,000 and \$5,682,000, respectively. For the six months ended June 30, 2009 and for the year ended December 31, 2008, the average balance of impaired non-accrual loans was \$6,962,000 and \$5,837,000, respectively. Approximately \$2,738,000 and \$2,294,000 of the allowance for loan losses were allocated against such impaired non-accrual loans, respectively, in accordance with SFAS 114 Accounting by Creditors for Impairment of a Loan an amendment of FASB Statement No. 5 and 15. The following is a summary of SBA loans held for investment as of:

<b>(In thousands):</b>	<b>June 30, 2009</b>	<b>December 31, 2008</b>
Due in one year or less	\$	\$ 61
Due between one and five years	1,455	1,417
Due after five years	28,474	30,465
 Total	 29,929	 31,943
Less: Allowance for loan losses	(3,756)	(3,420)
Less: Deferred origination fees, net	(1,610)	(1,611)
 Balance (net)	 \$ 24,563	 \$ 26,912

**NOTE 5 SERVICING ASSET:**

Servicing rights are recognized as assets when SBA loans are sold and the rights to service those loans are retained. The Company has adopted the provisions of SFAS 156 which requires all separately recognized servicing assets to be initially measured at fair value, if practicable. The Company reviews capitalized servicing rights for impairment which is performed based on risk strata, which are determined on a disaggregated basis given the predominant risk characteristics of the underlying loans. The predominant risk characteristics are loan term and year of loan origination.

The changes in the value of the Company's servicing rights for the six months ended June 30, 2009 were as follows:

<b>(In thousands):</b>	
Balance at December 31, 2008	\$ 2,282
Servicing assets capitalized	710
Servicing assets amortized	(398)
 Balance at June 30, 2009	 \$ 2,594

The estimated fair value of capitalized servicing rights was \$2,594,000 and \$2,282,000 at June 30, 2009 and December 31, 2008, respectively. The estimated fair value of servicing assets at both balance sheet dates was determined using a discount rate of 16.8%, weighted average prepayment speeds ranging from 1% to 18%, depending upon certain characteristics of the loan portfolio, a weighted average life of 3.2 years, and an average default rate of 5.0%.

The unpaid principal balances of loans serviced for others are not included in the accompanying condensed consolidated balance sheets. The unpaid principal balances of loans serviced for others were \$140,881,000 and \$141,587,000 as of June 30, 2009 and December 31, 2008, respectively.

**NOTE 6 LOSS PER SHARE:**

Basic loss per share is computed based on the weighted average number of common shares outstanding during the period. The dilutive effect of common share equivalents is included in the calculation of diluted loss per share only when the effect of their inclusion would be dilutive.



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The calculations of loss per share were:

(In thousands except per share data):	Three months Ended June 30:		Six months Ended June 30:	
	2009	2008	2009	2008
Numerator for basic and diluted EPS loss available to common shareholders	\$ (637)	\$ (1,982)	\$ (1,613)	\$ (4,676)
Denominator for basic and diluted EPS weighted average shares	35,625	35,750	35,625	35,809
Loss per share: Basic and diluted	\$ (0.02)	\$ (0.06)	\$ (0.05)	\$ (0.13)

The amount of anti-dilutive shares/units excluded from above is as follows:

Stock options	1,544	1,743	1,544	1,743
Warrants	266	216	266	216
Contingently issuable shares	97	474	97	474

**NOTE 7 SEGMENT REPORTING:**

Operating segments are organized internally primarily by the type of services provided, and in accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, the Company has aggregated similar operating segments into six reportable segments: Electronic payment processing, Web hosting, Small business finance, All other, Corporate and Capcos.

The Electronic payment processing segment is a processor of credit card transactions, as well as a marketer of credit card and check approval services to the small- and medium-sized business market. Expenses include direct costs (included in a separate line captioned electronic payment processing costs), professional fees, salaries and benefits, and other general and administrative costs, all of which are included in the respective caption on the condensed consolidated statements of operations.

The Web hosting segment consists of NTS, acquired in July 2004. NTS's revenues are derived primarily from web hosting services and consist of web hosting and set up fees. NTS generates expenses such as professional fees, payroll and benefits, and depreciation and amortization, which are included in the respective caption on the accompanying condensed consolidated statements of operations, as well as licenses and fees, rent, and general office expenses, all of which are included in other general and administrative costs in the respective caption on the condensed consolidated statements of operations.

The Small business finance segment consists of Small Business Lending, Inc., a lender that primarily originates, sells and services government guaranteed SBA 7(a) loans to qualifying small businesses through its licensed SBA lender; the Texas Whitestone Group which manages the Company's Texas Capco and closes loans; and NBC which provides accounts receivable financing, billing and accounts receivable maintenance services to businesses. NSBF generates revenues from sales of loans, servicing income for those loans retained to service by NSBF and interest income earned on the loans themselves. The lender generates expenses for interest, professional fees, salaries and benefits, depreciation and amortization, and provision for loan losses, all of which are included in the respective caption on the condensed consolidated statements of operations. NSBF also has expenses such as loan recovery expenses, loan processing costs, and other expenses that are all included in the other general and administrative costs caption on the condensed consolidated statements of operations.

The All Other segment includes revenues and expenses primarily from qualified businesses that received investments made through the Company's Capcos which cannot be aggregated with other operating segments. The two largest entities in the segment are Newtek Insurance Agency, LLC, an insurance sales operation, and Business Connect, LLC, a provider of sales and processing services.

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Corporate activities represent revenue and expenses not allocated to our segments. Revenue includes interest income and management fees earned from Capcos (and included in expenses in the Capco segment). Expenses primarily include corporate operations related to broad-based sales and marketing, legal, finance, information technology, corporate development and additional costs associated with administering the Capcos.

The Capco segment, which consists of the 15 Capcos, generates non-cash income from tax credits, interest income and gains from investments in qualified businesses which are included in other income. Expenses primarily include non-cash interest and insurance expense, management fees paid to Newtek (and included in the Corporate activities revenues), legal, and auditing fees and losses from investments in qualified businesses.

Management has considered the following characteristics when making its determination of its operating and reportable segments:

the nature of the product and services;

the type or class of customer for their products and services;

the methods used to distribute their products or provide their services; and

the nature of the regulatory environment (for example, banking, insurance, or public utilities).

The accounting policies of the segments are the same as those described in the summary of significant accounting policies.

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The following table presents the Company's segment information for the periods ended June 30, 2009 and 2008 and total assets as of June 30, 2009 and December 31, 2008 (In Thousands):

	For the three months ended June 30, 2009	For the three months ended June 30, 2008	For the six months ended June 30, 2009	For the six months ended June 30, 2008
<b>Third Party Revenue</b>				
Electronic payment processing	\$ 16,889	\$ 15,939	\$ 32,663	\$ 31,150
Web hosting	4,707	4,501	9,382	8,783
Small business finance	1,564	2,080	3,407	3,945
Capcos	2,733	1,602	4,311	3,238
All other	1,320	644	1,706	1,306
Corporate activities	925	2,487	1,785	3,560
<b>Total reportable segments</b>	<b>28,138</b>	<b>27,253</b>	<b>53,254</b>	<b>51,982</b>
Eliminations	(1,061)	(2,623)	(2,056)	(3,832)
<b>Consolidated Total</b>	<b>\$ 27,077</b>	<b>\$ 24,630</b>	<b>\$ 51,198</b>	<b>\$ 48,150</b>
<b>Inter-Segment Revenue</b>				
Electronic payment processing	\$ 51	\$ 18	\$ 96	\$ 36
Web hosting	87	39	200	78
Small business finance	22	761	36	769
Capcos	543	488	893	965
All other	135	182	275	359
Corporate activities	520	577	921	1,081
<b>Total reportable segments</b>	<b>1,358</b>	<b>2,065</b>	<b>2,421</b>	<b>3,288</b>
Eliminations	(1,358)	(2,065)	(2,421)	(3,288)
<b>Consolidated Total</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
<b>Income (loss) before benefit for income taxes</b>				
Electronic payment processing	\$ 1,060	\$ 1,167	\$ 2,023	\$ 2,247
Web hosting	917	737	1,833	1,351
Small business finance	(748)	(791)	(1,341)	(2,293)
Capcos	(1,063)	(2,859)	(2,167)	(4,344)
All other	555	(396)	151	(952)
Corporate activities	(1,496)	(487)	(3,352)	(2,673)
<b>Totals</b>	<b>\$ (775)</b>	<b>\$ (2,629)</b>	<b>\$ (2,853)</b>	<b>\$ (6,664)</b>
<b>Depreciation and amortization</b>				
Electronic payment processing	\$ 425	\$ 559	\$ 885	\$ 1,121
Web hosting	762	815	1,554	1,633
Small business finance	243	277	472	586
Capcos	(4)	14	12	24
All other	32	15	62	48
Corporate activities	112	86	234	164
<b>Totals</b>	<b>\$ 1,570</b>	<b>\$ 1,766</b>	<b>\$ 3,219</b>	<b>\$ 3,576</b>





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	As of June 30, 2009	As of December 31, 2008
<b>Identifiable assets</b>		
Electronic payment processing	\$ 14,742	\$ 15,432
Web hosting	13,078	14,080
Small business finance	40,606	48,361
Capcos	59,215	81,074
All other	7,056	7,515
Corporate activities	4,183	3,065
<b>Consolidated total</b>	<b>\$ 138,880</b>	<b>\$ 169,527</b>

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

*The following discussion and analysis of our financial condition and results of operations is intended to assist in the understanding and assessment of significant changes and trends related to the results of operations and financial position of the Company together with its subsidiaries. This discussion and analysis should be read in conjunction with the condensed consolidated financial statements and the accompanying notes.*

*This Quarterly Report on Form 10-Q contains forward-looking statements. Additional written or oral forward-looking statements may be made by Newtek from time to time in filings with the Securities and Exchange Commission or otherwise. The words believe, expect, seek, anticipate and intend and similar expressions identify forward-looking statements, which speak only as of the date the statement is made. Such forward-looking statements are within the meaning of that term in Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such statements may include, but are not limited to, projections of income or loss, expenditures, acquisitions, plans for future operations, financing needs or plans relating to our services, as well as assumptions relating to the foregoing. Forward-looking statements are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified. Future events and actual results could differ materially from those set forth in, contemplated by or underlying the forward-looking statements. Newtek does not undertake, and specifically disclaims, any obligation to publicly release the results of revisions which may be made to forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after such statements.*

*We also need to point out that our Capcos operate under a different set of rules in each of the 8 jurisdictions and that these place varying requirements on the structure of our investments. In some cases, particularly in Louisiana, we don't control the equity or management of a qualified business but that cannot always be presented orally or in written presentations.*

We directly distribute business services to small- and medium-sized businesses, a very significant marketplace in the United States. According to statistics published by the U.S. Small Business Administration, approximately 51% of the GDP and private sector employment in the United States comes from small businesses, and 99% of businesses in the United States which have one or more employees fit into this market segment. As of June 30, 2009, we had over 87,000 customer accounts. We use state-of-the-art web-based proprietary technology to be a low cost acquirer and provider of products and services to our small- and medium-sized business clients. We partner with Chartis (the property/casualty insurance companies of AIG), the Latino Coalition, Morgan Stanley, the Credit Union National Association with its 8,100 credit unions and 91 million members, Navy Federal Credit Union with 3.2 million members, Pershing, PSCU Financial Services, Inc., the nation's largest credit union service organization, and Fiserv Solutions, Inc. d/b/a IntegraSys, , all of whom have elected to offer certain of our business services and financial products rather than provide some or all of them directly for their customers. We have deemphasized our Capco business in favor of growing our operating businesses and do not anticipate creating any new Capcos in the foreseeable future.

For the quarter ended June 30, 2009, the Company substantially reduced its loss before benefit for income taxes to \$(775,000) from \$(2,629,000) in the same quarter of 2008. While this reduction in loss demonstrates improvements in operations with increases in revenue being matched to reductions in salaries and benefits, part of the reduction reflects the recovery of a \$1,000,000 related to an investment previously written off and shown in the All other segment. We had a net loss of \$(637,000), an improvement of \$1,345,000 over 2008, on revenues of \$27,077,000. Total revenues increased by \$2,447,000 or 10.0%, from

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\$24,630,000 for the quarter ended June 30, 2008 principally due to increased revenues in the Electronic payment processing, Web hosting, Capco, and All other segments offset by decreases in revenues from our Small business finance and Corporate activities segments. The reduction in the net loss of \$1,345,000 from the second quarter of 2008 reflects improvements in income from operations for the Web hosting segment from increased sales and a decrease in the losses for the Small business finance, Capco, All other, and Corporate segments offset by decreased income from operations for the Electronic payment processing segment. The decreased gross margin in Electronic payment processing primarily occurred during the slowing of the economy in the second half of 2008 and is anticipated to continue to negatively impact profitability for the segment throughout 2009. The improved net income in the Web hosting segment resulted from increased revenues combined with relatively stable expenses.

As a result of the dislocation in the secondary market for guaranteed loan sales, the Small business finance segment stopped originating new loans in the fourth quarter of 2008. Improving secondary market conditions and changes to the SBA 7(a) loan program in the 2<sup>nd</sup> quarter have permitted us to begin lending again, although the temporary nature of our lending line has caused management to limit the amount of loans we will originate. In June 2009, the Small business finance segment originated and sold a new loan at a premium. As of June 30, 2009, we had approximately \$16,327,000 outstanding under the \$30,000,000 GE line of credit of which the Company guarantees up to \$15,000,000 of the advances. On July 22, 2009 we entered into a Fifth Amendment and Consent (the Fifth Amendment ) to the Credit Agreement dated as of August 31, 2005 between NSBF and General Electric Capital Corporation (GECC) which made certain changes in the terms of the warehouse lending facility provided to NSBF. The Fifth Amendment reduces the aggregate total of the credit facility to \$15 million from \$28 million, adjusts the interest rate and other terms and extends the maturity date from August 31, 2009 to May 31, 2010 based upon progress shown by NSBF in obtaining a commitment for a replacement lender. The effectiveness of the Fifth Amendment is subject to the approval of the United States Small Business Administration. Upon the Fifth Amendment becoming effective the Company will have to partially pay the line down. There can be no assurance that we will be able to renew our credit line with GE, or that we will be able to negotiate an alternate arrangement. Failure to obtain replacement financing will have a material adverse effect on our business.

Improvement in operations and the investment recovery provided the Company with positive cash flow for the quarter and the first six months of 2009. Cash and cash equivalents increased to \$18,594,000 on June 30, 2009 from \$16,852,000 on December 31, 2008. Overall, we believe that throughout 2009 the Company will enjoy both the full year benefit from the expense reductions made in 2008 in the Small business finance, All other and Corporate segments as well as the continuing costs cutting efforts in 2009.

Our operating businesses are dependent on the health of the small- and medium-sized segments of the U.S. economy. The reduction in the availability of credit and a weakening economy could have a negative impact on consumer and commercial spending which could adversely impact Newtek's small business customers. This could also negatively impact the value of commercial and residential real estate, which could adversely impact the loan portfolio of our SBA Lending segment.

On August 13, 2008, the Company received a staff deficiency letter from The Nasdaq Stock Market ( Nasdaq ) indicating that, for the prior 30 consecutive days, the bid price for Newtek's common stock had closed below the minimum \$1.00 per share requirement for continued inclusion on the Nasdaq Global Market under Marketplace Rule 4450(a)(5) (the Rule ). In accordance with Marketplace Rule 4450(e)(2), the Company was given 180 calendar days, or until February 9, 2009, to regain compliance with the Rule. The letter also indicated that if the Company did not regain compliance by February 9, 2009, Nasdaq would provide written notification that Newtek's common stock will be delisted. On October 16, 2008, Nasdaq announced that it was suspending the rules requiring a minimum \$1.00 closing bid price and a minimum market value of publicly held shares until December 19, 2008, and on December 19, 2008 the suspension was extended until April 20, 2009, at which time the Rule will begin to run again. On July 13, 2009 the Company received another letter from the NASDAQ stating that the Company will have until November 27, 2009 to regain compliance. The Company can regain compliance, either during the suspension or during the compliance period resuming after the suspension, by achieving a \$1 closing bid price for a minimum of 10 consecutive trading days. At the current market price, the Company would not regain compliance, and there can be no assurance that the Company would be able to do so by November 27, 2009. If the Company is unable to regain compliance, it faces delisting. In the event that the common stock is delisted, there can be no assurance that an active public market for our stock can be sustained or that current trading levels can be sustained or not diminished.

Finally, in May 2009 the Company received a letter from the state of Florida stating that the Company's Florida capco, Wilshire Partners, LLC, had achieved 100% investment and therefore was eligible for final dissolution. Dissolution of the Capco will result in additional cost savings for the Company. In addition, as a result of meeting the conditions of its insurance policy, Wilshire Partners, LLC received a return of premium in the amount of \$250,000.

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**Electronic Payment Processing:** Credit card and debit card processing, check conversion and ACH solutions for the small- and medium-sized business market.

**Web Hosting:** CrystalTech Web Hosting, Inc., d/b/a/ Newtek Technology Services, which offers shared and dedicated web hosting and related services to the small- and medium-sized business market.

**Small Business Finance:** Newtek Small Business Finance, Inc., a nationally licensed, U.S. Small Business Administration lender that originates, sells and services loans to qualifying small businesses, which are partially guaranteed by the SBA. Texas Whitestone Group performs the closing function for all SBA 7(a) loans underwritten by NSBF. CDS Business Services, Inc. (d/b/a Newtek Business Credit) provides financing services to businesses by purchasing their receivables at a discounted rate. In addition, the Company provides billing and accounts receivable maintenance services to businesses.

**All Other:** Includes results from businesses formed from Investments in Qualified Businesses made through Capco programs which cannot be aggregated with other operating segments.

**Corporate Activities:** Corporate implements business strategy, directs marketing, provides technology oversight and guidance, coordinates and integrates activities of the segments, contracts with alliance partners, acquires customer opportunities and owns our proprietary NewTracker referral system. Revenue and expenses not allocated to our other segments, including interest income, Capco management fee income and corporate operations expenses.

**Capcos:** Fourteen certified capital companies, which invest in small- and medium-sized businesses. They generate non-cash income from tax credits and non-cash interest.

**Segment Results:**

The results of the Company's reportable segments for the three and six months ended June 30, 2009 and 2008 are discussed below.

**Electronic Payment Processing**

(In thousands):	Three months ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Electronic payment processing	\$ 16,880	\$ 15,921	\$ 959	6%
Interest income	9	18	(9)	(50)%
<b>Total revenue</b>	<b>16,889</b>	<b>15,939</b>	<b>950</b>	<b>6%</b>
<b>Expenses:</b>				
Electronic payment processing costs	14,107	12,925	1,182	9%
Salaries and benefits	991	977	14	1%
Professional fees	59	85	(26)	(31)%
Depreciation and amortization	425	559	(134)	(24)%
Other general and administrative costs	247	226	21	9%
<b>Total expenses</b>	<b>15,829</b>	<b>14,772</b>	<b>1,057</b>	<b>7%</b>
Income before benefit for income taxes	\$ 1,060	\$ 1,167	\$ (107)	(9)%

**Three months ending June 30, 2009 and 2008:**

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Electronic payment processing revenue increased \$959,000 or 6% between periods principally due to the overall impact of growth in organic revenue of approximately 8% while revenues from acquired portfolios decreased overall revenue growth by 2% between periods due to merchant attrition. Approximately 6% of the growth in organic revenue was derived from an increase in

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the average number of merchants under contract between years of 9%. However, the average monthly processing volume per merchant decreased 3% between years. The decrease in the average monthly processing volume per merchant in 2009 reflects a combination of a decrease in the average sales volume from existing merchants and the effect of new merchants added in 2009 being smaller in terms of average monthly processing volumes. The overall decrease in the average processing volume per merchant in 2009 we believe is primarily attributable to the recessionary economic environment in the United States. The remaining 2% increase in organic revenue is principally due to an increase in transaction count related fees. Total transactions processed increased 13% between years, including an increase in check card transactions of 18% between periods.

Electronic payment processing costs increased \$1,182,000 or 9% between years. Electronic payment processing cost resulting from acquired portfolios had the overall effect of decreasing such cost by approximately 2% between periods due to merchant attrition. Organic electronic payment processing costs had the effect of increasing total electronic payment processing costs by 11% between years. The revenues less electronic payment processing cost ( margin ) declined approximately 2.4% from 18.8% in 2008 to 16.4% in 2009. The 1.8% reduction in the margin was due to the increased residual payments made to certain third-party sales referral sources and the growth of such third-party sales on a sales mix basis. The remaining reduction in such margin between periods is principally due to the effects of competitive pricing pressures for new and existing merchants between years.

Excluding electronic payment processing costs, other costs decreased \$125,000 or 7% between years. Depreciation and amortization decreased \$134,000 between periods. The decrease in depreciation and amortization is principally due to a previously acquired portfolio intangible asset becoming fully amortized during 2009 and the effect between years of a portfolio impairment charge recorded in the fourth quarter of 2008. Remaining costs increased \$9,000 between years as the result of an increase in costs related to information technology and sales and marketing related services.

Income before benefit for income taxes decreased \$107,000 to \$1,060,000 in 2009 from \$1,167,000 in 2008. The decrease in income before benefit for income taxes in 2009 is principally due to the lower margin partially offset by an overall reduction in other costs between years.

(In thousands):	Six months ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Electronic payment processing	\$ 32,641	\$ 31,102	\$ 1,539	5%
Interest income	22	48	(26)	(54)%
<b>Total revenue</b>	<b>32,663</b>	<b>31,150</b>	<b>1,513</b>	<b>5%</b>
<b>Expenses:</b>				
Electronic payment processing costs	27,048	25,149	1,899	8%
Salaries and benefits	2,124	2,041	83	4%
Professional fees	114	152	(38)	(25)%
Depreciation and amortization	885	1,121	(236)	(21)%
Other general and administrative costs	469	440	29	7%
<b>Total expenses</b>	<b>30,640</b>	<b>28,903</b>	<b>1,737</b>	<b>6%</b>
Income before benefit for income taxes	\$ 2,023	\$ 2,247	\$ (224)	(10)%

**Six months ending June 30, 2009 and 2008:**

Electronic payment processing revenue increased \$1,539,000 or 5% between periods principally due to the overall impact of growth in organic revenue of approximately 6% while revenues from acquired portfolios decreased overall revenue growth by 1% between periods due to merchant attrition. Approximately 5% of the growth in organic revenue was derived from an increase in the average number of merchants under contract between years of 11%. However, the average monthly processing volume per merchant decreased 6% between years. The decrease in the average monthly processing volume per merchant in 2009 reflects a combination of a decrease in the average sales volume from existing merchants and the effect of new merchants added in 2009 being smaller in terms of average monthly processing volumes. The overall decrease in the average processing volume per merchant in 2009 we believe is primarily attributable to the recessionary economic environment in the

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United States. The remaining 1% increase in organic revenue is principally due to an increase in transaction count related fees. Total transactions processed increased 12% between years, including an increase in check card transactions of 21% between periods.

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Electronic payment processing costs increased \$1,899,000 or 8% between years. Electronic payment processing costs resulting from acquired portfolios had the overall effect of decreasing such cost by approximately 2% between periods due to merchant attrition. Organic electronic payment processing costs had the effect of increasing total electronic payment processing cost by 10% between years. The margin declined approximately 2.0% from 19.1% in 2008 to 17.1% in 2009. The 1.6% reduction in margin was due to increased residual payments made to certain third-party sales referral sources and the growth of such third-party sales on a sales mix basis. The remaining reduction in such margin between periods is principally due to the effects of competitive pricing pressures for new and existing merchants between years.

Excluding electronic payment processing costs, other costs decreased \$162,000 or 4% between years. Depreciation and amortization cost decreased \$236,000 between years. The decrease in depreciation and amortization cost is principally due to a previously acquired portfolio intangible asset becoming fully amortized during 2009 and the effect between years of a portfolio impairment charge recorded in the fourth quarter of 2008. Remaining costs increased \$74,000 between years as the result of an increase in the use and cost of services related to information technology and sales and marketing related services.

Income before benefit for income taxes decreased \$224,000 to \$2,023,000 in 2009 from \$2,247,000 in 2008. The decrease in income before benefit for income taxes in 2009 is principally due to the lower margin partially offset by an overall reduction in other costs between years.

**Web Hosting**

(In thousands):	Three months Ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Web hosting	\$ 4,702	\$ 4,499	\$ 203	5%
Interest income	5	2	3	150%
Total revenue	4,707	4,501	206	5%
<b>Expenses:</b>				
Salaries and benefits	1,245	1,218	27	2%
Interest	33	15	18	120%
Professional fees	28	28		%
Depreciation and amortization	762	815	(53)	(7)%
Other general and administrative costs	1,722	1,688	34	2%
Total expenses	3,790	3,764	26	1%
Income before benefit for income taxes	\$ 917	\$ 737	\$ 180	24%

**Three months ended June 30, 2009 and 2008:**

The segment derives revenue primarily from monthly recurring fees from hosting websites. Web hosting revenue between periods increased \$203,000, or 5%, to \$4,702,000 for the three months ended June 30, 2009 over the same period in 2008 due to a combination of improved revenue per website offsetting a decrease in the average number of hosted websites. Average monthly revenue per site increased 8% to \$23.84 from \$21.99. NTS utilized price increases coordinated with service and plan enhancements as well as new higher priced service offerings to help drive growth in revenue.

The total average number of sites for the three months ended June 30, 2009 as compared to the same period in 2008 decreased 2,442 sites, or 4%, to 65,727 from 68,169. A 2,503 or 4% decrease in average number of shared sites to 63,410 in 2009 from 65,913 in 2008 accounts for most of the lost sites; this recent trend of decreasing shared websites since the fourth quarter of 2008 reflects the effects of a deliberate price increase to improve profitability of the lowest priced plans as well as economic conditions and increased competition. The additional 147 average number of virtual dedicated websites in 2009, a new service offering which was not offered in the beginning of 2008, offset the decrease in the average number of total dedicated websites by 85 in 2009 as compared to 2008, or 4%, to 2,171 from 2,256. Although improvement in revenue per site reflects the greater growth in virtual dedicated sites in 2009 over 2008, which generate higher monthly fees versus higher end shared and lower end dedicated web hosting plans, revenues from shared and dedicated sites improved as well reflecting better pricing and utilization of higher



priced plans by customers.

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Total expenses increased 1% or \$26,000 to \$3,790,000 from \$3,764,000 for the three months ended June 30, 2009 as compared to the same period 2008. The increase in total expenses was due to a \$27,000 increase in salaries and benefits, a \$34,000 increase in other general and administrative costs mainly for marketing, and a \$18,000 increase in interest expense relating to the outstanding \$2.5 million note, offset in part by a \$53,000 decrease in depreciation and amortization.

Income before benefit for income taxes increased 24% or \$180,000 to \$917,000 for the three months ended June 30, 2009 from \$737,000 for the same period 2008. The improvement in profitability primarily resulted from increased web site plan revenue growing more quickly than the substantially fixed costs of the datacenter; imbedded rent, utility and software licensing fees effectively contributed more revenue. Maintenance of current staffing levels since the third and fourth quarter of 2008 contributed to the improvement in income as well. Due to management's focus on cost efficiency, continued growth in revenue should result in improved future profits and margins.

(In thousands):	Six months ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Web hosting	\$ 9,374	\$ 8,775	\$ 599	7%
Interest income	8	8		%
<b>Total revenue</b>	<b>9,382</b>	<b>8,783</b>	<b>599</b>	<b>7%</b>
<b>Expenses:</b>				
Salaries and benefits	2,430	2,413	17	1%
Interest	67	31	36	116%
Professional fees	109	54	55	102%
Depreciation and amortization	1,554	1,633	(79)	(5)%
Other general and administrative costs	3,389	3,301	88	3%
<b>Total expenses</b>	<b>7,549</b>	<b>7,432</b>	<b>117</b>	<b>2%</b>
<b>Income before benefit for income taxes</b>	<b>\$ 1,833</b>	<b>\$ 1,351</b>	<b>\$ 482</b>	<b>36%</b>

**Six months ended June 30, 2009 and 2008:**

The segment derives revenue primarily from monthly recurring fees from hosting websites. Web hosting revenue between periods increased \$599,000, or 7%, to \$9,374,000 for the six months ended June 30, 2009 over the same period 2008 due to improved revenue per website and organic growth of hosted virtual websites, which was a new service offering successfully launched in the third quarter of 2008. NTS utilized sales promotions and service and plan enhancements to help drive growth in sites and revenue.

The increase in revenue reflects a decrease in the average number of total websites by 1,321 for the six months ended June 30, 2009 as compared to the same period in 2008, or 2%, to 66,268 from 67,589 as well as an increase in average monthly revenue per site of 9% to \$23.57 from \$21.64. Improvement in revenue per site primarily reflects the greater growth in virtual dedicated sites, the customers gravitating towards higher end services combined with additional options, and is also a result of a price change to our lowest priced plan in the third quarter of 2008. The average number of dedicated websites, which generate a higher monthly fee versus shared websites, decreased by 8 between periods, or less than 1%, to an average of 2,206 per month from an average of 2,214 per month for the same period in 2008. The average number of shared websites decreased 1,434, or 2%, to an average of 63,941 per month for the six months ended June 30, 2009, from an average of 65,375 per month for the same period 2008. The decreasing trend in total shared and dedicated site counts began in the fourth quarter of 2008. This change in trend reflects the continuing economic conditions, which started impacting the web hosting segment in the fourth quarter of 2008, along with increased competition, a deliberate price increase by the hosting division to improve profitability of the lowest priced plans, and the move of high-end shared users and low-end dedicated users to the new Hyper-V plan.

Total segment expenses increased at 2%, or \$117,000, as compared to the 7%, or \$599,000, growth in revenues for the six months ended June 30, 2009. The majority of the 2% or \$117,000 increase in expenses between periods reflects an increase in other general and administrative costs of \$88,000, an increase in salaries and benefits of \$17,000, an increase in interest expense of \$36,000, and an increase in professional fees of \$55,000 offset by a decrease in depreciation and amortization expense of \$79,000. As a percent of sales, other general and administrative

costs, depreciation and amortization, and salaries and benefits

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have decreased between periods as a result of management's efforts to maintain and improve cost efficiency. The increase in other general and administrative costs was primarily due to a \$143,000 increase in marketing, a result of banner ads, search engine optimization and click advertisement, and a \$50,000 increase in bad debt expense, mainly attributable to the poor economic environment. The increases in marketing and bad debt expenses were offset in part by a \$31,000 decrease in utilities and communications, a result of renegotiations of internet and telephone contracts, and an approximate decrease of \$70,000 in office related expenses. Salaries and benefits increased \$17,000, at a lower rate than revenue growth. The \$79,000 decrease in depreciation and amortization was primarily due to the slowing of capital expenditures as a result of consolidation efforts in the shared segment to allow for more efficient use of the already existing equipment within the datacenter. The increase of \$55,000 in professional fees was due to higher audit and legal fees in the six months ended June 30, 2009.

Income before benefit for income taxes increased 36% or \$482,000 to \$1,833,000 for the six months ended June 30, 2009 from \$1,351,000 for the six months ended June 30, 2008. The improvement in profitability primarily resulted from increased web site plan sales, while, imbedded rent, utility and software licensing fees effectively contributed more revenue. Maintenance of current staffing levels and other general and administrative cost in the first six months of 2009 contributed to the improvement in income as well. Due to management's focus on cost efficiency, continued growth in revenue should result in improved future profits and margins.

**Small Business Finance**

(In thousands):	Three months ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Premium income	\$ 137	\$ 326	\$ (189)	(58)%
Servicing fee	424	438	(14)	(3)%
Interest income	376	658	(282)	(43)%
Management fees	146	146		
Other income	481	512	(31)	(6)%
<b>Total revenue</b>	<b>1,564</b>	<b>2,080</b>	<b>(516)</b>	<b>(25)%</b>
<b>Expenses:</b>				
Salaries and benefits	705	1,159	(454)	(39)%
Interest	374	454	(80)	(18)%
Management fees	115	115		
Professional fees	88	80	8	10%
Depreciation and amortization	243	277	(34)	(12)%
Provision for loan losses	509	472	37	8%
Other general and administrative costs	278	314	(36)	(11)%
<b>Total expenses</b>	<b>2,312</b>	<b>2,871</b>	<b>(559)</b>	<b>(19)%</b>
<b>Loss before benefit for income taxes</b>	<b>\$ (748)</b>	<b>\$ (791)</b>	<b>\$ (43)</b>	<b>(5)%</b>

**Three months ended June 30, 2009 and 2008:**

Revenue is derived primarily from premium on loan sales generated by the sale of the guaranteed and unguaranteed portions of SBA loans, interest income on SBA loans held for investment, servicing fee income on the guaranteed portions of SBA loans previously sold, servicing income for loans originated by other lenders for which NSBF is the servicer, and receivables factoring and billing services, classified as other income above, provided by Newtek Business Credit ( NBC ). Most SBA loans originated by NSBF charge an interest rate equal to the Prime rate plus an additional percentage amount; the interest rate resets to the current Prime rate on a monthly or quarterly basis which will result in changes to the amount of interest accrued for that month and going forward and a re-amortization of a loan's payment amount until maturity.

As a result of the dislocation in the secondary market for guaranteed loan sales, NSBF stopped originating new loans in the fourth quarter of 2008. Improving secondary market conditions and changes to the SBA 7(a) loan program in the 2<sup>nd</sup> quarter



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have permitted NSBF to begin lending again, although the temporary nature of its lending line, described below, has caused management to limit the amount of loans NSBF will make. One new loan was originated in June 2009, resulting in the sale of one \$1,500,000 guaranteed portion in the three months ended June 30, 2009, compared to 22 guaranteed portions sold aggregating \$7,346,000 in the same period for the prior year. The Company does not expect to generate material premium income until NSBF begins to originate new loans in substantial volumes. Premium income for the three months ended June 30, 2009 also included the sale of a \$400,000 loan classified as held for investment and the discount recognized thereon. NSBF sold the loan at par with the carrying value below the amount sold of \$27,000 being recorded as premium income. This \$27,000 represented the allocated portion of the remaining discount recorded at the time of loan origination.

Servicing fee income related to SBA loans decreased by \$14,000 due to a decrease in the NSBF loan servicing portfolio and an increase in non-performing loans, as well as a reduction in the fee income associated with the servicing of an SBA portfolio for a savings bank in New York which totaled \$36,000 for the three months ended June 30, 2009 compared to \$41,000 in the three months ended June 30, 2008. The average NSBF servicing portfolio for the quarter ended June 30, 2009 was \$126,356,000 compared with \$127,654,000 for the quarter ended June 30, 2008.

Interest income decreased by \$282,000 due primarily to a decrease in the average interest rate being charged to borrowers from 7.9% to 5.9% due to a reduction in the prime rate, a decrease in the average outstanding portfolio from \$32,397,000 in the three months ended June 30, 2008 to \$30,098,000 in the three months ended June 30, 2009, and an increase in the nonperforming NSBF portfolio from an average of 18.5% to 24.2% for the three months ended June 30, 2008 and 2009, respectively. If NSBF does not originate and fund new loans in substantial volumes, then its performing portfolio will continue to shrink as loans normally pay down principal and default, further reducing its opportunity to earn interest and servicing income.

Other income decreased by \$31,000 due to a decrease in revenue earned by NSBF of \$43,000 attributable to a decrease in the number of loans prepaying as well as a decrease in revenue earned on late payments. Additionally, in the three months ended June 30, 2008, Small Business Lending, the holding company for NSBF recognized \$60,000 in referral fee income compared to no corresponding revenue earned in 2009. These decreases in revenue were offset by an increase in revenue earned by Newtek Business Credit. For the three months ended June 30, 2009, NBC had revenue of \$372,000 and purchased \$5,955,000 of receivables from an average customer base of 120 compared to revenue of \$319,000 on \$4,257,000 of receivables purchased with an average customer base of 124 for the three months ended June 30, 2008.

Consideration in arriving at the provision for loan loss includes past and current loss experience, current portfolio composition, future estimated cash flows, and the evaluation of real estate and other collateral as well as current economic conditions. The quarterly provision for loan loss increased slightly quarter over quarter by \$37,000. Our reserve for loan losses as compared to our gross portfolio balance increased from \$2,484,000 or 7.75% at June 30, 2008 to \$3,755,000 or 12.71% at June 30, 2009. At June 30, 2009 and June 30, 2008, total impaired non-accrual loans amounted to \$7,126,000 and \$5,908,000, respectively, with \$2,738,000 or 38.0% and \$1,284,000 or 21.7% of the allowance for loan losses being allocated against such impaired non-accrual loans, respectively. The year over year increase in the reserve balance on an absolute and as a percentage of impaired non-accrual loans reflects the effects the recession has had on NSBF's borrowers and the borrowers assets underlying the loans

Salaries and benefits decreased by \$454,000 as a result of staffing cutbacks in sales and origination staff in connection with the lending operation totaling \$513,000 that began in the fourth quarter of 2008 and were completed during the quarter ended March 31, 2009. NSBF believes it currently has adequate staff to service its portfolio and originate loans in the future if it chooses to do so. This was offset by an increase in headcount and salaries at NBC of \$59,000 for the same period. Combined headcount decreased over 39% from 51 at June 30, 2008, to 31 at June 30, 2009.

Professional fees for the three months ended June 30, 2009 increased by \$8,000 primarily due to increases in audit and tax related expenses partially offset by a reduction in 3<sup>rd</sup> party consulting expenses.

After deducting the amortization of deferred financing costs associated with the lines of credit held by NSBF and NBC of \$131,000 for the three months ended June 30, 2008 and \$89,000 for the three months ended June 30, 2009, interest expense decreased from \$323,000 to \$285,000 for the same periods, respectively. This decrease was attributable to a decrease in the prime lending rate on which the financing costs are based from an average of 5.08% to a rate of 3.25% quarter over quarter. This decrease in the Prime rate was offset by an increase in the spread over prime being charged by General Electric ( GE ). In 2008, the spread over Prime was 0.25% whereas in the three months ending June 30, 2009, the spread was 2.50%. This increase in the spread was offset by a decrease in the average amount outstanding under the GE credit facility. The average amount outstanding for the three months ended June 30, 2008 was \$19,843,000 as compared with \$15,663,000 during the same period in 2009.



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Other general and administrative costs decreased by \$36,000 due primarily to a reduction in forced placed insurance costs, a reduction in bank service charges and an overall reduction in office related expenses due to a reduction in headcount at NSBF and cost cutting measures at NBC. These cost reductions were partially offset by a \$57,000 increase in loan recovery expenses as a result of the increase in non-performing portfolio.

Overall, the reduction in segment expenses of \$559,000 balanced out the \$516,000 reduction in segment revenue, resulting in a slight improvement in loss before benefit of income taxes for the three months ended June 30, 2009 versus that of June 30, 2008.

(In thousands):	Six months ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Premium income	\$ 582	\$ 476	\$ 106	22%
Servicing fee	825	922	(97)	(11)%
Interest income	796	1,344	(548)	(41)%
Management fees	293	293		
Other income	911	910	1	0%
<b>Total revenue</b>	<b>3,407</b>	<b>3,945</b>	<b>(538)</b>	<b>(14)%</b>
<b>Expenses:</b>				
Salaries and benefits	1,447	2,462	(1,015)	(41)%
Interest	792	956	(164)	(17)%
Management fees	230	230		
Professional fees	158	219	(61)	(28)%
Depreciation and amortization	472	586	(114)	(19)%
Provision for loan losses	933	911	22	2%
Other general and administrative costs	716	874	(158)	(18)%
<b>Total expenses</b>	<b>4,748</b>	<b>6,238</b>	<b>(1,490)</b>	<b>(24)%</b>
<b>Loss before benefit for income taxes</b>	<b>\$ (1,341)</b>	<b>\$ (2,293)</b>	<b>\$ (952)</b>	<b>(42)%</b>

**For the six months ended June 30, 2009 and 2008:**

Revenue is derived primarily from premium on loan sales generated by the sale of the guaranteed and unguaranteed portions of SBA loans, interest income on SBA loans held for investment, servicing fee income on the guaranteed portions of SBA loans previously sold, servicing income for loans originated by other lenders for which NSBF is the servicer, and receivable factoring and billing services, classified as other income above, provided by Newtek Business Credit ( NBC ). Most SBA loans originated by NSBF charge an interest rate equal to the Prime rate plus an additional percentage amount; the interest rate resets to the current Prime rate on a monthly or quarterly basis which will result in changes to the amount of interest accrued for that month and going forward and a re-amortization of a loan's payment amount until maturity.

NSBF stopped originating new loans in the fourth quarter of 2008 although loan fundings continued through the first quarter of 2009 along with one additional new origination in the second quarter of 2009. First six months 2009 premium income, and its increase over the same period in 2008, benefited primarily from a change in the method of valuing servicing assets created at the time of sale. The Company sold 14 guaranteed loans in the six months ended June 30, 2009, aggregating \$8,802,000 compared to 35 loans sold aggregating \$9,818,000 in the same period for the prior year. With the exception of one new loan originated in June 2009, the period's sales primarily consisted of loans funded over previous quarters that had been held for sale due to capital market conditions. The Company does not expect to generate material premium income until NSBF begins to originate new loans in substantial volumes. As a result of the dislocation in the secondary market for guaranteed loan sales through April 2009, premiums on guaranteed loan sales dropped from an average of 107.6% with 1% servicing in the six months ended June 30, 2008 to an average of 102.4% with 1% servicing through March 31, 2009. As a result of this decrease, management made the business decision to sell its guaranteed loans available for sale through March 31, 2009 at par with an average of 3.4% servicing. In June 2009, with the secondary market returning to somewhat normalized levels, the Company sold





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one newly originated guaranteed loan aggregating \$1,500,000 at a premium of 107.55%. To more appropriately value the servicing asset created under current secondary market conditions, management utilized a discounted cash flow model, which uses valuation techniques to convert future amounts to a single present amount and is based on the value indicated by current market expectations about those future amounts. The premium earned on those loans sold at par reflects the valuation of the newly created servicing assets, not cash earned at the time of the sales.

Premium income for the six months ended June 30, 2009 also included the sale of a \$400,000 loan classified as held for investment and the discount recognized thereon. NSBF sold the loan at par with the carrying value below the amount sold of \$27,000 being recorded as premium income. This \$27,000 represented the allocated portion of the remaining discount recorded at the time of loan origination. There were no corresponding sales during the six months ended June 30, 2008.

Servicing fee income related to SBA loans decreased by \$97,000 due to a decrease in the NSBF loan servicing portfolio and an increase in non-performing loans, as well as a reduction in the fee income associated with the servicing of an SBA portfolio for a savings bank in New York which totaled \$74,000 for the six months ended June 30, 2009 compared to \$87,000 in the six months ended June 30, 2008. The average NSBF servicing portfolio for the six months ended June 30, 2009 was \$127,319,000 compared with \$130,062,000 for the six months ended June 30, 2008 while the nonperforming servicing portfolio increased from \$17,434,000 at June 30, 2008 to \$29,715,000 at June 30, 2009.

Interest income decreased by \$548,000 due primarily to a decrease in the average interest rate being charged to borrowers from 8.81% to 5.93% due to a reduction in the prime rate, a decrease in the average outstanding portfolio from \$32,533,000 in the six months ended June 30, 2008 to \$31,205,000 in the six months ended June 30, 2009, and an increase in the nonperforming portfolio from an average of 19.0% of the NSBF portfolio to 22.0% for the six months ended June 30, 2008 and 2009, respectively. If NSBF does not originate and fund new loans in substantial volumes, then its performing portfolio will continue to shrink as loans normally pay down principal and default, further reducing its opportunity to earn interest and servicing income.

Other income increased by \$1,000 due to an increase in revenue earned by Newtek Business Credit. For the six months ended June 30, 2009, NBC had revenue of \$732,000 and purchased \$10,377,000 of receivables from an average customer base of 122 compared to revenue of \$623,000 on \$7,191,000 of receivables purchases with an average customer base of 121 for the six months ended June 30, 2008. This increase was offset by a decrease in revenue earned by NSBF in the amount of \$57,000 attributable to a decrease in the number of loans prepaying as well as a decrease in revenue earned on late payments and revenue earned on loan originations, offset by an increase in income recognized on recoveries. Additionally, in the six months ended June 30, 2008, Small Business Lending, the holding company for NSBF recognized \$60,000 in referral fee income compared to \$9,000 of corresponding revenue earned in 2009.

Consideration in arriving at the provision for loan loss includes past and current loss experience, current portfolio composition, future estimated cash flows, and the evaluation of real estate and other collateral as well as current economic conditions. The provision for loan loss increased slightly period over period by \$22,000. Our reserve for loan losses as compared to our gross portfolio balance increased from \$2,484,000 or 7.75% at June 30, 2008 to \$3,755,000 or 12.71% at June 30, 2009. At June 30, 2009 and June 30, 2008, total impaired non-accrual loans amounted to \$7,126,000 and \$5,908,000, respectively with \$2,738,000 or 38.0% and \$1,284,000 or 21.7% of the allowance for loan losses being allocated against such impaired non-accrual loans, respectively. The year over year increase in the reserve balance on an absolute and as a percentage of impaired non-accrual loans reflects the effects the recession has had on NSBF's borrowers and the borrowers' assets underlying the loans.

Salaries and benefits decreased by \$1,015,000 as a result of staffing cutbacks in sales and origination staff in connection with the lending operation totaling \$1,052,000 that began in the fourth quarter of 2008 and were completed during the quarter ended March 31, 2009. NSBF believes it currently has adequate staff to service its portfolio and originate loans in the future if it chooses to do so. This was offset by an increase in headcount and salaries at NBC of \$35,000 for the same period. Combined headcount decreased over 39% from 51 at June 30, 2008, to 31 at June 30, 2009.

Professional fees for the six months ended June 30, 2009 decreased by \$61,000 primarily due to decreases in the utilization of outside consultants as well as a decrease in the timing of audit and tax related expenses partially offset by an increase in contingent expenses.

After deducting the amortization of deferred financing costs associated with the lines of credit held by NSBF and NBC of \$262,000 for the six months ended June 30, 2008 and \$196,000 for the six months ended June 30, 2009, interest expense decreased from \$694,000 to \$596,000 for the same periods, respectively. This decrease was attributable to a decrease in the

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prime lending rate on which the financing costs are based from a weighted average of 5.65% to a rate of 3.25% period over period. This decrease in the Prime rate was offset by an increase in the spread over prime being charged by GE. In 2008, the spread over Prime was 0.25% whereas in the six months ending June 30, 2009, the weighted average spread was 2.38%. This increase in the spread was offset by a decrease in the average amount outstanding under the GE credit facility. The average amount outstanding for the six months ended June 30, 2008 was \$19,009,000 as compared with \$16,581,000 during the same period in 2009.

Other general and administrative costs decreased by \$158,000 due primarily to an overall reduction in office and overhead related expenses due to a reduction in headcount at NSBF and cost cutting measures at NBC. The Company also experienced a reduction in loan processing fees due to the suspension of loan originations. These cost reductions were partially offset by an \$188,000 increase in loan recovery expenses as a result of the increase in non-performing loans and the loss experienced on several REO properties due to the impact of falling real estate prices.

Although segment revenues fell \$538,000 or 14% period over period primarily because of the performance of NSBF, the Company's cost cutting efforts successfully reduced segment expenses by \$1,490,000 or 24%, reducing the loss before benefit of income taxes by \$(952,000) or 42% to \$(1,341,000) for the six months ended June 30, 2009 from a loss of \$(2,293,000) for the six months ended June 30, 2008. The segment should continue to benefit from cost reductions for the remainder of 2009.

**Capcos**

(In thousands):	Three months Ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Income from tax credits	\$ 2,714	\$ 1,491	\$ 1,223	82%
Interest income	19	111	(92)	(83)%
<b>Total revenue</b>	<b>2,733</b>	<b>1,602</b>	<b>1,131</b>	<b>71%</b>
<b>Expenses:</b>				
Interest	3,197	1,709	1,488	87%
Management fees	947	2,508	(1,561)	(62)%
Professional fees	143	205	(62)	(30)%
Other than temporary decline in value of investments	158		158	100%
Other general and administrative costs	(176)	100	(276)	(276)%
<b>Total expenses</b>	<b>4,269</b>	<b>4,522</b>	<b>(253)</b>	<b>(6)%</b>
Loss before fair market value adjustment and benefit for income taxes	(1,536)	(2,920)	(1,384)	(47)%
Net change in fair market value of Credits in lieu of cash and Notes payable in credits in lieu of cash	473	61	412	675%
<b>Loss before benefit for income taxes</b>	<b>\$ (1,063)</b>	<b>\$ (2,859)</b>	<b>\$ (1,796)</b>	<b>(63)%</b>

**Three months ending June 30, 2009 and 2008:**

As described in Note 3 to the condensed consolidated financial statements, effective January 1, 2008, the Company adopted SFAS 157 concurrent with its adoption of SFAS 159 for substantially all credits in lieu of cash, notes payable in credits in lieu of cash and prepaid insurance. These are the financial assets and liability associated with the Company's Capco notes that are reported within the Company's Capco segment. The table above reflects the effects of the adoption of fair value measurement on the income and expense items (income from tax credits, interest expense and insurance expense) related to the revalued financial assets and liability for the three months ended June 30, 2009 and 2008. In addition, the net change to the revalued financial assets and liability for the three months ended June 30, 2009 and 2008 is reported in the line Net change in fair market value of Credits in lieu of cash and Notes payable in credits in lieu of cash.

Revenue is derived primarily from non-cash income from tax credits. The increase in income from tax credits for the second quarter 2009 revenue versus the second quarter 2008, reflects the effect of the higher interest rate used under fair value accounting. The amount of future revenue will fluctuate with future interest rates. However, over future periods, the amount of tax credits, and therefore the income the Company

will recognize, will decrease to zero.

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Expenses consist primarily of management fees and non-cash interest expense. Management fees decreased 62%, or \$1,561,000, to \$947,000 for the three months ended June 30, 2009 from \$2,508,000 for the same period ended 2008. The primary reason for the decline was due to a recovery, and therefore increase, of management fees from one Capco totaling approximately \$1,538,000 in the previous period in 2008. Management fees, which are eliminated on consolidation, are expected to decline in the future as the Capcos mature and utilize their cash. Interest expense increased 87%, or \$1,488,000, to \$3,197,000 for the three months ended June 30, 2009 from \$1,709,000 for the same period last year, reflecting the higher interest rate used under fair value accounting. Other general and administrative costs decreased by \$276,000 due to the returned premium on a Capco insurance policy which expired in April 2009, in the amount of \$250,000.

Because the Company does not anticipate creating any new Capcos in the foreseeable future, the Capco segment will continue to incur losses going forward. The Capcos will continue to earn cash investment income on their cash balances and incur cash management fees and operating expenses. The amount of cash available for investment and to pay management fees will be primarily dependent upon future returns generated from investments in qualified businesses. Income from tax credits will consist solely of accretion of the discounted value of the declining dollar amount of tax credits the Capcos will receive in the future; the Capcos will continue to incur non-cash interest expense.

(In thousands):	Six months ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Income from tax credits	\$ 4,250	\$ 2,954	\$ 1,296	44%
Interest income	61	280	(219)	(78)%
Other income		4	(4)	(100)%
<b>Total revenue</b>	<b>4,311</b>	<b>3,238</b>	<b>1,073</b>	<b>33%</b>
<b>Expenses:</b>				
Interest	5,260	3,462	1,798	52%
Management fees	1,827	3,602	(1,775)	(49)%
Professional fees	295	381	(86)	(23)%
Other than temporary decline in value of investments	158		158	100%
Other general and administrative costs	(52)	198	(250)	(126)%
<b>Total expenses</b>	<b>7,488</b>	<b>7,643</b>	<b>(155)</b>	<b>2%</b>
<b>Loss before fair market value adjustment and benefit for income taxes</b>	<b>(3,177)</b>	<b>(4,405)</b>	<b>(1,228)</b>	<b>(28)%</b>
Net change in fair market value of Credits in lieu of cash and Notes payable in credits in lieu of cash	1,010	61	949	1,556%
<b>Loss before benefit for income taxes</b>	<b>\$ (2,167)</b>	<b>\$ (4,344)</b>	<b>\$ (2,177)</b>	<b>(50)%</b>

**Six months ending June 30, 2009 and 2008:**

As described in Note 3 to the condensed consolidated financial statements, effective January 1, 2008, the Company adopted SFAS 157 concurrent with its adoption of SFAS 159 for substantially all credits in lieu of cash, notes payable in credits in lieu of cash and prepaid insurance. These are the financial assets and liability associated with the Company's Capco notes that are reported within the Company's Capco segment. The table above reflects the effects of the adoption of fair value measurement on the income and expense items (income from tax credits, interest expense and insurance expense) related to the revalued financial assets and liability for the six months ended June 30, 2009 and 2008. In addition, the net change to the revalued financial assets and liability for the six months ended June 30, 2009 and 2008 is reported in the line Net change in fair market value of Credits in lieu of cash and Notes payable in credits in lieu of cash.

Revenue is derived primarily from non-cash income from tax credits. The increase in income from tax credits revenue for the six months ended June 30, 2009 versus the same period in 2008 reflects the effect of the higher interest rate used under fair value accounting than that previously used under cost basis accounting. The amount of future income from tax credits revenue will fluctuate with future interest rates. However, over future periods, the amount of tax credits, and therefore the income the Company will recognize, will decrease to zero.



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Other general and administrative costs decreased by \$250,000 or 126% due to the returned premium on a Capco insurance policy which expired in April 2009, in the amount of \$250,000.

Expenses consist primarily of management fees and non-cash interest expense. Management fees decreased 49%, or \$1,775,000, to \$1,827,000 for the six month period ended June 30, 2009 from \$3,602,000 during the same period of 2008. The decrease was primarily due to the recovery of management fees from one Capco totaling approximately \$1,638,000 during the six months ended June 30, 2008. Management fees, which are eliminated on consolidation, are expected to continue to decline in the future as the Capcos mature and utilize their cash. Interest expense increased 52%, or \$1,798,000, to \$5,260,000 for the six months ended June 30, 2009 from \$3,462,000 for the same period last year reflecting the higher interest rate used under fair value accounting.

Because the Company does not anticipate creating any new Capcos in the foreseeable future, we anticipate that our Capco segment will incur losses going forward through 2010. The Capcos will continue to earn cash investment income on their cash balances and incur cash management fees and operating expenses. The amount of cash available for investment and to pay management fees will be primarily dependent upon future returns generated from investments in qualified businesses. Income from tax credits will consist solely of accretion of the discounted value of the declining dollar amount of tax credits the Capcos will receive in the future; the Capcos will continue to incur non-cash interest expense.

**All Other**

(In thousands):	Three months Ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Interest income	\$ 12	\$ 35	\$ (23)	(66)%
Insurance commissions	217	350	(133)	(38)%
Other income	1,091	259	832	321%
<b>Total revenue</b>	<b>1,320</b>	<b>644</b>	<b>676</b>	<b>105%</b>
<b>Expenses:</b>				
Salaries and benefits	402	819	(417)	(51)%
Professional fees	46	(37)	83	224%
Depreciation and amortization	32	15	17	113%
Other general and administrative costs	285	243	42	17%
<b>Total expenses</b>	<b>765</b>	<b>1,040</b>	<b>(275)</b>	<b>(26)%</b>
Income (loss) before benefit for income taxes	\$ 555	\$ (396)	\$ 951	240%

**Three months ending June 30, 2009 and 2008:**

The All Other segment includes revenues and expense primarily from qualified businesses that received investments made through the Company's Capcos which cannot be aggregated with other operating segments.

The revenue increase of \$676,000 is primarily due to the increase in other income of \$832,000 in the second quarter 2009 as compared to the second quarter of 2008. The increase in other income was primarily due to a \$1,000,000 recovery in the second quarter of 2009 related to a qualified investment previously written off as compared to a recovery in the second quarter of 2008 of only \$41,000. Insurance commissions decreased by \$133,000 for the three month period ended June 30, 2009 as compared to the three month period ended June 30, 2008, due primarily to staff reduction and reorganization negatively impacting new insurance sales as well as current economic conditions reducing both the demand for new policies as well as coverage levels for existing customers. Interest income decreased as a result of a decrease in cash and cash equivalents during the first second of 2009 as compared with the second quarter of 2008.

Salaries and benefits decreased by \$417,000, or 51% to \$402,000 for the three months ended June 30, 2009, as compared to \$819,000 for same period 2008, as a result of staff reductions in the insurance agency and other entities. The increase in professional fees of \$83,000, or 224% to \$46,000 for second quarter ended 2009 as compared to \$(37,000) for 2008 was mainly due to a one-time reversal of broker commissions in the

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second quarter of 2008. Other general administrative costs increased by \$42,000, or 17% to \$285,000 for the second quarter ended 2009, as compared to \$243,000 for 2008.



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Income (loss) before benefit for income taxes increased by \$951,000 during the second quarter of 2009 as compared with the second quarter of 2008, primarily due to the increase in revenues of \$676,000 and the decrease in total expenses of \$275,000.

(In thousands):	Six months Ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Interest income	\$ 28	\$ 108	\$ (80)	(74)%
Insurance commissions	417	593	(176)	(30)%
Other income	1,261	605	656	108%
<b>Total revenue</b>	<b>1,706</b>	<b>1,306</b>	<b>400</b>	<b>31%</b>
<b>Expenses:</b>				
Salaries and benefits	894	1,670	(776)	(46)%
Professional fees	125	70	55	79%
Depreciation and amortization	62	48	14	29%
Other general and administrative costs	474	470	4	1%
<b>Total expenses</b>	<b>1,555</b>	<b>2,258</b>	<b>(703)</b>	<b>(31)%</b>
Income (loss) before benefit for income taxes	\$ 151	\$ (952)	\$ 1,103	116%

**Six months ending June 30, 2009 and 2008:**

The All Other segment includes revenues and expense primarily from qualified businesses that received investments made through the Company's Capcos which cannot be aggregated with other operating segments.

Revenue increased \$400,000, or 31%, for the six months ended June 30, 2009 as compared to the six months ended June 30, 2008. The revenue increase consists of a \$656,000 increase in other income primarily due to a \$1,000,000 recovery in the second quarter of 2009 related to a qualified investment previously written off, offset by a \$176,000 decrease in insurance commissions and an \$80,000 decrease in interest income. The decrease in insurance commissions for the three month period ended June 30, 2009 as compared to the three month period ended June 30, 2008 was due primarily to staff reduction and reorganization negatively impacting new insurance sales as well as current economic conditions reducing both the demand for new policies as well as coverage levels for existing customers. Interest income decreased as a result of a decrease in cash and cash equivalents during the first six months of 2009 as compared with the first six months of 2008.

Salaries and benefits decreased by \$776,000, or 46% to \$894,000 for the six months ended June 30, 2009, as compared to \$1,670,000 for same period 2008, as a result of staff reductions in the insurance agency and other entities. The increase in professional fees of \$55,000, or 79% to \$125,000 for the six months ended June 30, 2009 as compared to \$70,000 for the same period in 2008 was mainly due to a one-time reversal of broker commissions in the second quarter of 2008.

Income (loss) before benefit for income taxes increased by \$1,103,000 during the six months ended June 30, 2009 as compared with the six months ended June 30, 2008, primarily due to the increase in revenues of \$400,000 and the decrease in total expenses of \$703,000.

**Corporate activities**

(In thousands):	Three months ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Management fees	\$ 916	\$ 2,477	\$ (1,561)	(63)%

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Interest income	9	6	3	50%
Other income		4	(4)	(100)%
<b>Total revenue</b>	<b>925</b>	<b>2,487</b>	<b>(1,562)</b>	<b>(63)%</b>
Expenses:				
Salaries and benefits	1,154	1,812	(658)	(36)%
Professional fees	574	317	257	81%
Depreciation and amortization	112	86	26	30%
Other general and administrative costs	581	759	(178)	(23)%
<b>Total expenses</b>	<b>2,421</b>	<b>2,974</b>	<b>(553)</b>	<b>(19)%</b>
Loss before benefit for income taxes	\$ (1,496)	\$ (487)	\$ 1,009	207%

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Revenue is derived primarily from management fees earned from the Capcos, which amount to 2.5% of certified capital. Management fee revenue declined 63%, or \$1,561,000, to \$916,000 for the three months ended June 30, 2009 from \$2,477,000 for the second quarter of 2008. The net decrease was primarily due to the recovery of management fees from one Capco totaling approximately \$1,538,000 during the three months ended June 30, 2008. Management fees, which are eliminated on consolidation, are expected to decline in the future as the Capcos mature and utilize their cash. If a Capco does not have current or projected cash sufficient to pay management fees, then such fees are not accrued.

Expenses declined \$553,000, or 19%, in the second quarter of 2009 from the comparable period in 2008. As a result of the Company's cost cutting initiatives, salaries and benefits decreased \$658,000 or 36% to \$1,154,000 for the second quarter of 2009 as compared to \$1,812,000 for the same period ended 2008. The Company expects Salaries and benefits to remain static or slightly decline from its current level over the remainder of 2009. The Company does not believe that the reductions will impact the management of the Company's businesses. Professional fees increased \$257,000, or 81%, in the second quarter of 2009 from the comparable period in 2008 due to the Company exploring various financing and restructuring alternatives and as a result incurred significant one-time professional fees for the period.

(In thousands):	Six months ended June 30:		\$ Change	% Change
	2009	2008		
<b>Revenue:</b>				
Management fees	\$ 1,764	\$ 3,540	\$ (1,776)	(50)%
Interest income	12	16	(4)	(25)%
Other income	9	4	5	125%
<b>Total revenue</b>	<b>1,785</b>	<b>3,560</b>	<b>(1,775)</b>	<b>(50)%</b>
<b>Expenses:</b>				
Salaries and benefits	2,393	3,978	(1,585)	(40)%
Professional fees	1,139	644	495	77%
Depreciation and amortization	234	164	70	43%
Other general and administrative costs	1,371	1,447	(76)	(5)%
<b>Total expenses</b>	<b>5,137</b>	<b>6,233</b>	<b>(1,096)</b>	<b>(18)%</b>
Loss before benefit for income taxes	\$ (3,352)	\$ (2,673)	\$ 679	25%

**Six months ended June 30, 2009 and 2008:**

Revenue is derived primarily from management fees earned from the Capcos, which amount to 2.5% of certified capital. Management fee revenue decreased 50%, or \$1,776,000, to \$1,764,000 for the six month period ended June 30, 2009 from \$3,540,000 during the same period of 2008. The decrease was primarily due to the recovery of management fees from one Capco totaling approximately \$1,638,000 during the six months ended June 30, 2008. Management fees, which are eliminated on consolidation, are expected to decline in the future as the Capcos mature and utilize their cash. If a Capco does not have current or projected cash sufficient to pay management fees then such fees are not accrued.

Expenses declined \$1,096,000, or 18%, during the six month period ended June 30, 2009 from the comparable period in 2008. As a result of the Company's cost cutting initiatives, salaries and benefits decreased \$1,585,000 or 40% to \$2,393,000 for the six months ended June 30, 2009 as compared to \$3,978,000 for the same period ended 2008. The Company expects Salaries and benefits to remain static or slightly decline from its current level over the remainder of 2009. The Company does not believe

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that the reductions will impact the management of the Company's businesses. Professional fees increased \$495,000, or 77%, for the six months ended June 30, 2009 from the comparable period in 2008 due to the Company exploring various financing and restructuring alternatives and as a result incurred significant one-time professional fees for the period.

**Critical Accounting Policies and Estimates:**

The Company's significant accounting policies are described in Note 1 of the Notes to Condensed Consolidated Financial Statements included in its Form 10-K for the fiscal year ended December 31, 2008. A discussion of the Company's critical accounting policies, and the related estimates, are included in Management's Discussion and Analysis of Results of Operations and Financial Position in its Form 10-K for the fiscal year ended December 31, 2008.

**Liquidity and Capital Resources**

(Dollars in thousands)

	<b>For the six months ended June 30,</b>	
	<b>2009</b>	<b>2008</b>
Net cash provided by (used in) operating activities	\$ 4,649	\$ (10,882)
Net cash provided by (used in) investing activities	2,337	(1,764)
Net cash (used in) provided by financing activities	(5,244)	4,220
Net increase (decrease) in cash and cash equivalents	1,742	(8,426)
Cash and cash equivalents, beginning of period	16,852	25,372
Cash and cash equivalents, end of period	\$ 18,594	\$ 16,946

Cash requirements and liquidity needs over the next twelve months are anticipated to be funded primarily through operating results and available cash and cash equivalents. The Company also has the capacity to borrow from the \$10 million Capital One line of credit through NTS for working capital needs and acquisitions. Amounts currently borrowed under the Capital One line of credit will convert to a term loan in September, 2009; the Company is currently in discussions with Capital One regarding extending the termination date of the revolving features of the line. The Small business finance segment depends on outside funding sources to finance loan origination and receivable purchases. The SBA lending unit funds its cash requirements and liquidity needs through available cash and cash equivalents but primarily utilizes the \$15 million GE line of credit to originate and warehouse the guaranteed and unguaranteed portion of SBA loans. On July 22, 2009 NSBF entered into a Fifth Amendment and Consent (the Fifth Amendment) to the Credit Agreement dated as of August 31, 2005 between NSBF and General Electric Capital Corporation (GECC) which has made certain changes in the terms of the warehouse lending facility provided to NSBF. The Fifth Amendment reduces the aggregate total of the credit facility to \$15 million, adjusts the interest rate and other terms and extends the maturity date from August 30, 2009 to May 31, 2010 based upon progress shown by NSBF in obtaining a commitment for a replacement lender. The effectiveness of the Fifth Amendment is subject to the approval of the United States Small Business Administration. GE has indicated to the Company that GE no longer intends to provide credit facilities to finance companies. Therefore there can be no assurance that the Company will be able to renew the credit line with GE or that it will be able to negotiate an alternate arrangement. Failure to obtain financing would have a material adverse effect on our business. The receivables financing unit utilizes the \$10 million Wells Fargo line of credit to purchase receivables. There are no cross covenants or collateralization under any of the above lending facilities. The availability of the lending facilities is subject to the compliance with certain covenants and in addition, for the GE and Wells Fargo lines, the amount of collateral and collateral requirements, as set forth in the agreements. The Company guarantees the lines of credit for the subsidiaries: Capital One for the amount borrowed, GE up to \$15 million, and Wells Fargo up to \$800,000. As of June 30, 2009, the Company's unused sources of liquidity consisted of \$18,594,000 in unrestricted cash and cash equivalents, and \$7,500,000, \$982,000 and \$299,000 available through the Capital One, GE, and Wells Fargo lines of credit, respectively.

Restricted cash totaling \$8,273,000, which is primarily held in the Capcos, can be used in managing and operating the Capcos, making qualified investments, to repay debt obligations and for the payment of income taxes.

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Net cash flows provided by operating activities increased \$15,531,000 to \$4,649,000 for the six months ended June 30, 2009 as compared to \$(10,882,000) for the six months ended June 30, 2008. This net increase was primarily due to a decrease of \$3,063,000 in the net loss period over period, an \$8,308,000 decrease in the originations of SBA loans held for sale, as well as a \$4,397,000 decrease in the broker receivable.

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Net cash flows provided by investing activities primarily includes the purchase of fixed assets and customer accounts, activity regarding the unguaranteed portions of SBA loans, changes in restricted cash and activities involving investments in qualified businesses. Net cash flows provided by investing activities increased by \$4,101,000 to \$2,337,000 for the six months ended June 30, 2009 compared to \$(1,764,000) for the six months ended June 30, 2008. The increase was due primarily to greater returns of investments in qualified businesses of \$1,112,000 for the six months ended June 30, 2009 as compared to the same period last year, and a \$1,119,000 decrease in the purchase of fixed assets and customer merchant accounts as well as a decrease of \$2,631,000 in the amount of SBA loans originated for investment. In addition, \$1,469,000 of restricted cash became available, or declined, in 2008 versus an increase in the change in restricted cash of \$107,000 in 2009.

Net cash flows used in financing activities primarily includes repayments on notes payable to Capital One, Wells Fargo, and GE. Net cash flows used in financing activities increased by \$9,464,000 to \$(5,244,000) for the six months ended June 30, 2009 from \$4,220,000 for the six months ended June 30, 2008. The primary reason was due to net repayments on bank notes payable of \$(5,203,000) during the six month period ended June 30, 2009 as compared to net borrowings of \$5,157,000 in 2008.

Newtek funds its holding company through cash on-hand, cash flow from operating businesses, and the receipt of annual management fees from the Capcos equal to 2.5% of initial funding. However, the management fees do not represent revenues to Newtek on a consolidated basis as this is a transfer of funds from Newtek's Capcos to the holding company, and all intercompany transactions and balances are eliminated in consolidation. These fees from Capcos are expected to decrease over the next few years as the Capcos mature in their business cycle. The Company does not intend to add new Capcos and will rely on expanding the operations of its underlying businesses and cutting costs at the holding company to maintain liquidity. If the operating companies do not continue to grow as expected to produce significant cash flow surpluses, if the capital markets should be inaccessible to Newtek, and if other borrowings are unavailable, the Company will experience a decrease in its liquidity and would be forced to diminish materially its operations so as to conform its expenditures to the cash then available.

Newtek expects to finance other ventures principally with existing funds or new additional borrowings under current or future bank facilities.

**Item 3. Quantitative and Qualitative Disclosure about Market Risk.**

All of our business activities contain elements of risk. We consider the principal types of risk to be fluctuations in interest rates and loan portfolio valuations. We consider the management of risk essential to conducting our businesses. Accordingly, risk management systems and procedures are designed to identify and analyze our risks, to set appropriate policies and limits and to continually monitor these risks and limits by means of reliable administrative and information systems and other policies and programs.

Because the SBA lender borrows money to make loans and investments, our net operating income is dependent upon the difference between the rate at which we borrow funds and the rate at which we invest these funds. The Company has outstanding bank notes payable of approximately \$16,327,000 at June 30, 2009. Under the fourth amendment signed in December 2008, the interest rate on such notes is variable, based on the current Prime rate plus 2.0% or three month LIBOR plus 4.00%, whichever is higher. Such interest rates increase by 0.25% each quarter beginning January 1, 2009. As of June 30, 2009, the interest rate being charged to NSBF is 5.75%. On July 22, 2009 we entered into a Fifth Amendment and Consent (the Fifth Amendment) to the Credit Agreement with GECC which made certain changes in the terms of the warehouse lending facility provided to NSBF. The Fifth Amendment reduces the aggregate total of the credit facility to \$15 million from \$28 million, adjusts the interest rate and other terms and extends the maturity date from August 31, 2009 to May 31, 2010 based upon progress shown by NSBF in obtaining a commitment for a replacement lender. There can be no assurance that we will be able to renew or extend our credit line with GE, or that we will be able to negotiate an alternate arrangement. Failure to obtain financing would have a material adverse effect on our business.

There can be no assurance that a significant change in market interest rates will not have a material adverse effect on our interest income. In periods of sharply rising interest rates, our cost of funds would increase, which would reduce our net operating income. We have analyzed the potential impact of changes in interest rates on interest income net of interest expense. Assuming that the balance sheet were to remain constant and no actions were taken to alter the existing interest rate sensitivity, a hypothetical immediate 1% change in interest rates would have the effect of a net increase (decrease) in assets by less than 1% for 2009. Although management believes that this measure is indicative of our sensitivity to interest rate changes, it does not adjust

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for potential changes in credit quality, size and composition of the assets on the balance sheet, and other business developments that could affect a net increase (decrease) in assets. Accordingly, no assurances can be given that actual results would not differ materially from the potential outcome simulated by this estimate.

Additionally, we do not have significant exposure to changing interest rates on invested cash which was approximately \$26,867,000 at June 30, 2009. We do not purchase or hold derivative financial instruments for trading purposes. All of our transactions are conducted in U.S. dollars and we do not have any foreign currency or foreign exchange risk. We do not trade commodities or have any commodity price risk.

We believe that we have placed our demand deposits, cash investments and their equivalents with high credit-quality financial institutions. Invested cash is held almost exclusively at financial institutions with ratings from Standard and Poor's of A- or better. The Company invests cash not held in interest free checking accounts or bank money market accounts mainly in U.S. Treasury only money market instruments or funds and other investment-grade securities. As of June 30, 2009, cash deposits in excess of FDIC and SIPC insurance totaled approximately \$6,227,000 and funds held in U.S. Treasury only money market funds or equivalents in excess of SIPC insurance totaled approximately \$9,766,000.

**Item 4. Controls and Procedures.**

(a) Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures as of the end of the period covered by this report are functioning effectively to provide reasonable assurance that the information required to be disclosed by us in reports filed under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Securities Exchange Act is accumulated and communicated to the issuer's management including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. A controls system, no matter how well designed and operated, cannot provide absolute assurance that the objectives of the controls systems are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

(b) Change in Internal Control over Financial Reporting

No change in our internal control over financial reporting occurred during the quarter ended June 30, 2009 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

(c) Limitations

A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurances that the control system's objectives will be met. Furthermore, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple errors or mistakes. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with its policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. We periodically evaluate our internal controls and make changes to improve them.

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**PART II OTHER INFORMATION**

**Item 1. Legal Proceedings**

We are not involved in any material pending litigation. We and/or one or more of our investee companies are involved in lawsuits regarding wrongful termination claims by employees or consultants, none of which are individually or in the aggregate material to Newtek.

**Item 6. Exhibits**

<b>Exhibit No.</b>	<b>Description</b>
10.7.4	Fifth Amendment and Waiver to Credit Agreement dated July 21, 2009 to the Credit Agreement dated August 31, 2005, between Newtek Business Services, Inc., the other credit parties signatory thereto and General Electric Capital Corporation (Incorporated by reference to Exhibit 99.1 to Newtek's Report on Form 8-K, filed July 23, 2009).
31.1	Certification by Chief Executive Officer required by Rule 13a-14(a) and 15d-14(a) under the Exchange Act.
31.2	Certification by Chief Financial Officer required by Rule 13a-14(a) and 15d-14(a) under the Exchange Act.
32.1	Certification by Chief Executive and Chief Financial Officers pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.



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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**NEWTEK BUSINESS SERVICES, INC.**

Date: August 13, 2009

By: /s/ Barry Sloane  
Barry Sloane  
Chairman of the Board, Chief Executive Officer and Secretary

Date: August 13, 2009

By: /s/ Seth A. Cohen  
Seth A. Cohen  
Chief Financial Officer and Treasurer