

**CALIFORNIA INFRASTRUCTURE AND ECONOMIC DEVELOPMENT BANK
(IBank)**

**SMALL BUSINESS FINANCE CENTER
SMALL BUSINESS LOAN GUARANTEE PROGRAM (SBLGP)
STAFF REPORT**

DIRECTIVES AND REQUIREMENTS

ISSUE:

The Small Business Financial Assistance Act of 2013 (Law) requires the IBank Board of Directors (Board) to adopt Directives and Requirements (Directives and Requirements) for the implementation of programs administered under the Small Business Finance Center within IBank by June 1, 2015. These proposed Directives and Requirements, attached hereto as Exhibit A, primarily affect the State and Federally funded Small Business Loan Guarantee Programs (SBLGP), yet also address direct loan programs such as the Farm Loan Program, the Surety Bond Guarantee Program, and the Secondary Market for Guaranteed Loans, all of which are subject areas of the Small Business Finance Center as a result of the transferred administration of the Small Business Loan Guarantee Programs from the Business, Transportation and Housing Agency (BT&H) to IBank. In the event that other subject areas under the program or other financing products are offered by the Small Business Finance Center in the future, Directives and Requirements may be supplemented to address those new subject areas and financing products. Following are the Proposed Directives and Requirements to be vetted for Board adoption. In accordance with the Law, these Directives and Requirements replace all existing or prior regulations promulgated with respect to the programs from BT&H. Upon adoption of the Directives and Requirements by the Board, the aforementioned regulations will no longer be in effect.

BACKGROUND:

The California Small Business Loan Guarantee Program (SBLGP) was established in 1968 to create jobs and opportunities for small businesses, targeting those owned by minorities, women, and disabled persons. IBank promotes local economic development by providing guarantees for SBLGP loans issued to small businesses from financial institutions, typically banks, that otherwise may not be approved. As a result of the SBLGP, participating small businesses are able to secure financing that allows them to grow and expand their business. The loan guarantee serves as a credit enhancement and an incentive for financial institutions to make loans to small businesses that otherwise may not be able to obtain financing.

In addition to guarantees for term loans and lines of credit, the SBLGP features emergency guarantees to assist businesses in the event of a natural disaster, and direct farm loans to help growers who cannot obtain conventional bank financing. The farm loans are guaranteed by the U. S. Department of Agriculture.

The SBLGP was approved to receive \$84.2 million in federal funds from the U.S. Treasury under the State Small Business Credit Initiative (SSBCI), a component of President Obama's Small Business Jobs Act of 2010. The SSBCI funds have unique requirements. Consequently, the SSBCI funded loan guarantees are administered separately as a subset of the SBLGP (and are referred to here as the Federal Program). Thus, since 2011, the Program has consisted of two subsets: the state-funded portion of the Program (SBLGP or State Program) and the federal SSBCI-funded portion (Federal Program). The Federal Program is the primary fund source and program being utilized at this time. The State Program is used as a backup since some rules differ between the two subsets of the Program.

When Assembly Bill No. 1247 passed in October of 2013, it transferred the administration of the Small Business Loan Guarantee Programs from the Business, Transportation and Housing Agency (BT&H) to the IBank. The proposed adoption of the Directives and Requirements are intended to preserve its legacy programs still being utilized and provide a streamlined and compliant process for the guarantees of loans to small businesses in California that provide economic expansion and job creation. Although the funding for the subsets of the Program will remain separate, it is the intent of the Directives and Requirements to create a continuity of similarity for both the Federal Program and the State Program which will give a much needed update to the State program policies to bring them in line with the Federal program. In addition, the proposed Directives and Requirements will provide a seamless transition for the consolidation of the state and federal programs in 2017.

ANALYSIS:

The Small Business Financial Assistance Act Government Code Sections 63089 calls for the IBank Board to adopt directives and requirements concerning the implementation of the chapter and pursuant to Chapter 1 (commencing with Section 14000) of Part 5 of Division 3 of Title 1 of the Corporations Code. Any regulations adopted pursuant to Chapter 1 (commencing with Section 14000) of Part 5 of Division 3 of Title 1 of the Corporations Code, as that chapter read on January 1, 2013, shall remain in effect until the IBank Board adopts directives and requirements relating to the specific policy or activity, but in no case beyond June 1, 2015.

The SBLGP staff collaborated with the nine participating Financial Development Corporations (FDCs or Corporations) that administer the programs to create new policy and procedures. In addition, this Proposal was sent to stakeholders and posted on the IBank website with a request for written comments for a 30 day period. Recognizing the inconsistency between the federal and state program rules causes confusion, it is proposed that uniformity and clarity through Directives and Requirements be implemented as soon as possible.

For the ease of the program administration, IBank will produce the Directive and Requirements of the program in its entirety in a document that is based on the previous BT&H regulations and will incorporate the changes the IBank Board adopts (Exhibit A). Following are the proposed requirements, amendments and clarifications.

Recommendation:

Staff recommends approval of the Resolution 15-08 in connection with the following Directives and Requirements for the Small Business Finance Center programs, including the Small Business Loan Guarantee Program, the direct lending Farm Loan Program, the Bond Guarantee Program and the Secondary Market for Guaranteed Loans.

Proposed Directives and Requirements:

Section numbers below refer to Government Code (as part of the Law). Provisions of the SBLGP Directives and Requirements are those sections numbered in the 5000s.

1. **63088.3 (p) and 63089.36(b)(1) and 63089.56.(c)(6) and 63089.70.(c)(5) and 63089.80.(g)(5) and 63089.95(d)**

The Proposed Directives and Requirements establish that results of a small business loan guarantee, a surety bond guarantee, a direct loan or other debt instrument issued, must be the creation or retention of at least one full time equivalent (FTE) and a non-profit must also employ at least one FTE. Although the Directives and Requirements adopted by the IBank Board should establish guidelines as to the preferred ratio of jobs created or retained to total funds borrowed, IBank is providing guidance in the form of a unit measurement rather than a ratio. A ratio of jobs to total funds borrowed would disqualify many who need access to capital the most. Using a unit of at least one job created or retained will ensure acceptance of single owner operated businesses. The current federal program tracks FTEs and requires at least one full time equivalent employee when funds are used to support a loan to a business or non-profit organization. Following this methodology will create unity amongst the programs. The program was originally established to create jobs; however, the program also strives to encourage economic development by supporting small businesses that retain jobs.

2. **5000(f)(4)**

The Proposed Directives and Requirements expand the definition of a Small Business to include a non-profit that employs at least one full time equivalent employee. The federal program allows non-profits that are borrowing for business purposes to participate. Permissible borrowers include state-designated charitable, religious, or other non-profit or eleemosynary institutions, government-owned corporations, consumer and marketing cooperatives, and faith-based organizations provided the loan is for a "business purpose". Present regulations do not address non-profits one way or the other, yet IBank finds these organizations vital to job creation and retention.

3. **63088.5 and 5002(b)(12)**

The Proposed Directives and Requirement amends the maximum loan amount for the Loan Guarantee Program to \$20 million with a maximum guarantee of \$2.5 million when using State funds, in the absence of Federal funds, used to support the guarantee. The current state policy supports loans up to \$1 million. This limitation has been in effect for many years and has created an underutilization of the state program. The present maximum for a federally supported loan is up to \$20 million with a maximum guarantee amount of \$2.5 million. Loans with a guarantee equal to or greater than \$1 million require a peer review.

Raising the maximum will allow IBank to support larger numbers of small businesses in need of capital. The Executive Director would also reserve the right to accept a request for a loan larger than \$20 million on a case by case basis and offer specific written approval. The guarantee would still be restricted to \$2.5 million and would only be allowable when guaranteed with State funds. IBank does not want to discourage loans in the SBLGP that may not fit other programs for small businesses.

4. **63089.80(h) and 5110 (d) (5)**

The Proposed Directives and Requirement sets the maximum loan amount of a direct loan or other debt instrument amount not to exceed \$1,392,000. The direct loan program being utilized through IBank is the Farm Loan Program. The program allows Corporations to lend the State's funds for farm ownership or operations and those loans are guaranteed up to 90% by USDA. The maximum loan amount matches the criteria used by the USDA Farm Service Agency Guaranteed Farm Loan Program.

5. **63089.80(h) and 5118**

The Proposed Directives and Requirement sets the maximum net fee amount of a direct loan or other debt instrument amount not to exceed two percent (2%). The direct loan program being utilized through IBank is the Farm Loan Program. The program allows Corporations to charge fees for Farm Loans. The maximum fee amount matches the criteria used by the USDA Farm Service Agency Guaranteed Farm Loan Program.

6. **63088.5 and 5002(b)(1)**

The Proposed Directives and Requirement amends the maximum guarantee amount of 80% for loans and microloans. It also proposes the Executive Director have the authority to lower the guarantee amount if it is found necessary to preserve the fund. In order to help balance the increase in maximum loan amounts, it is proposed the percentage of guarantee be lowered. The federal program only allows guarantees up to 80% of the loan amount with a requirement the lender be 20% at risk. This is a reduction in the percentage previously allowed, yet this practice has been accepted by the FDCs and no reports of loss of business have occurred as a consequence. In the event the fund begins to diminish it may be necessary to lower the guarantee amount in order to preserve the fund, therefore sustaining the program for a longer period of time.

7. **The Proposed Directive and Requirement sets criteria that a Corporation in existence less than 5 years adheres to the same Directives and Requirements of all Corporations.**

The Law provides that the proposed Directives and Requirements may treat Corporations in existence less than five (5) years differently. IBank asserts that the criteria for Corporation participation is accommodating enough that a Corporation in existence less than five years should comply on the same level as seasoned Corporations, except for Corporations subject to a probationary period as indicated in Corporations Code Section 14012.

8. **63089.56(d)**

The Proposed Directive and Requirement sets criteria that a Corporation in existence less than 5 years adheres to the same rules as seasoned FDCs for the basis of transferring account funds to those corporations. Since the trust funds will be pooled amongst all FDCs,

newer FDCs have the advantage of participating in a well-established fund and therefore should be held to the same standards and criteria requirements as established FDCs.

9. **63089.3(b)(1) and 63089.56(d)**

The Proposed Directive and Requirement sets criteria that a Corporation is to maintain a default rate of less than 5% of all of its outstanding guarantees. The present policy for default rate is based on a five year floating average net, which only reflects state supported guarantees and not federal supported guarantees. These criteria will account for the entire portfolio of each Corporation's outstanding loan balances.

10. **63089.3(b)(1) and 63089.56(d)**

The Proposed Directive and Requirement sets criteria that a Corporation must enroll at least one federally supported guarantee, or in the absence of federal funds, one state fund supported guarantee per fiscal year. There is a need for criteria to ensure Corporations are participating and efforts are being made to utilize the program, however; IBank recognizes the productivity of a corporation is often forced to operate in situations of an unpredictable lending climate, unfortunate geographic economic status, lack of personnel, and low population of its territory. There is an expectation of productivity and effort, yet IBank will keep the criteria to a minimum so as not to penalize corporations with meager results due to no fault of their own.

11. **63089.3(o)**

The Proposed Directives and Requirement sets criteria that while the funds of a corporation's trust fund account reside in the expansion fund, use of the principal on the funds shall be governed by the same use of funds in Government Code section 63089.5(b). Since it is the intent to pool the trust fund, it is unlikely a corporation's trust fund would reside in the expansion fund. If this were to occur, the fund would be used for previously established purposes.

12. **63089.57**

The Proposed Directives and Requirement clarifies that return on funds from investments may be used for program purposes, including administrative expenses of the Bank and/or the Corporations, at the Executive Directors discretion. In the past, earnings from funds deposited to the trust fund have been distributed to the FDCs for administrative costs. It should be clarified this is not an entitlement of the FDC and the distribution of funds will be for program purposes including administrative costs at the discretion of the Executive Director. IBank has not utilized the funds from investment for its administrative costs in the past, yet would like to reserve the option to do so.

13. **63089.58**

The Proposed Directive and Requirement clarifies that the Program Manager may create a trust fund account to be shared by multiple Corporations (pooled account) for program uses. The designation of an individual trust fund or a shared trust fund account will be determined by the Program Manager and written in the contract. It is the intent of IBank to pool the individual Corporation trust accounts to replicate the present federal program. Funds designated to the Farm Loan Program may remain in individual accounts for the Corporations participating in the Farm Loan Program or may be pooled.

14. 63089.67

The Proposed Directives and Requirement establishes that the Executive Director will have authority to determine and amend the amount of the fees, up to 3%, no more than twice in each fiscal year. The Corporation will charge a documentation fee of \$250.00 per loan guarantee and a fee of up to 3% of the guarantee amount for each guarantee. An FDC does not have the authority to waive a fee or charge more or less than the amount determined as written in the FDC contract. The Corporation will not charge an annual servicing fee on loan guarantees. Historically, the fees charged by the FDCs to borrowers for loans have been established in policy or regulation. With changing markets and products it seems practical to allow this decision at the program management level. The current schedule dictates fees "up to" a certain amount which creates competition amongst the FDCs. FDCs were meant to be territorial rather than competitive. There is also an established annual servicing fee authorization that need be eliminated as it is routinely waived and does not serve the needs of this market.

15. 63089.70(c)(4) and 63089.80(g)(4) and 63089.95(c)

The Proposed Directive and Requirement sets criteria that a borrower of a loan guaranteed under the program, a direct loan, or a bond guarantee have at least \$1.00 of equity interest in the business at the time of the loan. The programs are designed to encourage entrepreneurship and provide capital access to women, minorities and veterans. Microloans, small start-up businesses and businesses with sweat equity may not have large equity interests. Lenders will likely follow stricter criteria, yet IBank does not want to be so restrictive that it discourages lending to those in real need of capital.

16. 63089.80(b)

The Proposed Directive and Requirement specifies the amount of funds available for direct lending, including yet not limited to Farm Loans is twenty percent (20%) of the aggregate trust fund(s) available for the Small Business Finance Center State lending programs. The Farm Loan program is the only direct lending program at this time. Twenty percent (20%) of the total fund is sufficient for the current demands of the program, while not creating a shortage of funds for other lending programs utilizing the fund.

17. 63089.97(d)

The Proposed Directives and Requirement clarifies that Corporations must provide any and all documents related to the Small Business Finance Center Programs that are required or requested by the Program Manager or Executive Director within the deadline given. IBank has specific quarterly and annual deadlines to meet for reporting and audit requests in regard to its federally supported loan guarantees. IBank must adhere to a retention period for all documents related to a federally funded guarantee until January 1, 2020. In addition legislative representatives often call on IBank to provide immediate information. It is vital the Corporations, who act as agents of the state, respond to IBank's request for information when requested.

18. **The Proposed Directives and Requirement clarifies that Corporations must adhere to the State Small Business Credit Initiative (SSBCI) rules and guidance when supporting a guarantee with federal funds. The rules and guidance include, but are not limited to the following resources; the Small Business Jobs Act of 2010, the California Allocation Agreement, SSBCI Policy Guidance, National Standards for Compliance and Oversight, and the SSBCI F.A.Q's.**
19. **The Proposed Directives and Requirement clarifies that IBank will preserve Small Business Loan Guarantee legacy programs currently in existence including subject areas for the Farm Loan Program, Surety Bond Guarantee Program, and the Secondary Market for Guaranteed Loans.** When Assembly Bill No. 1247 passed in October of 2013, it transferred the administration of the Small Business Loan Guarantee Programs from Business, Transportation and Housing Agency (BT&H) to IBank. There are subject areas under the programs that did not have specific Directives and Requirements requested, yet IBank is including them in the Directives and Requirements in order to preserve the policies for such subject areas that have been, are, or will be utilized within the Small Business Finance Center.

The following attachments are the Directives and Requirements for the respective subject areas that were previously addressed in the BT&H regulations. BT&H regulations are being incorporated (except as otherwise amended by these Directives and Requirements) into the Directives and Requirements for the Small Business Finance Center. These Directives and Requirements may be amended or supplemented from time to time by the IBank Board.

Attachment A: Surety Bond Guarantees

Attachment B: Secondary Market for Guaranteed Portion of Loans

Attachment C: Farm Loans

EXHIBIT A

Directives and Requirements
For the
Small Business Finance Center
Small Business Loan Guarantee Programs
Adopted May 26, 2015

§ 5000. Definitions.

The following Directives and Requirements are adopted pursuant to the Small Business Financial Assistance Act of 2013 (California Government Code 63088 and following and California Corporations Code sections 14000 and following) and replace all existing regulations for the Small Business Financial Assistance Act of 2013 Loan Guarantee Programs (SBLGP). These Directives and Requirements may apply to future programs or financing products or new Directives and Requirements may be adopted, as determined by the IBank Board that may be offered by the Small Business Finance Center pursuant to the Law. In the event of any inconsistency between these Directives and Requirements and the Law, the provisions of the Law shall govern. To the extent that the Law is changed subsequent to the date of the adoption of these Directives and Requirements, these shall be deemed amended to bring them in conformity with the Law.

The following definitions supplement those provided by the Law and shall govern the construction of these Directives and Requirements:

(a) "Allocation" and "Allocated" mean the process of disbursing appropriated Expansion Fund moneys to a Corporation's trust fund account, except for Allocations for areas affected by a state of emergency or a disaster, which shall be disbursed pursuant to Corporations Code section 14037.6. The Allocation process is described in subsections 5070(a) through (c).

(b) "Application" means all of the information required by a Lender or Surety in order to determine whether to offer a Borrower a Loan, or a Principal a Bond.

(c) "Bond" means an obligation in writing concerning the construction or service work of Principal, binding the Surety to pay certain sums upon the occurrence of specified events connected to the payment of sums due by the Principal pursuant to a payment bond, and the obligation to complete the construction or service work, pursuant to a performance bond.

(d) "Bond Guarantee" means a Guarantee which promises the payment of all or a portion of a Claim.

(e) "Bond Line" means a specified amount and term of Bond Guarantee authority which Principal is authorized to apply against any Bond with a specified Surety during the term of the Bond Line.

(f) "Borrower" means an eligible business which has received a commitment for a Loan, or has prepared an Application. In order to be an "eligible business, the business must be either:

(1) a "Small Business" as defined in part 121 of chapter 1 of title 13 of the Code of Federal Regulations as amended;

(2) a Farm Enterprise; or

(3) a non-profit organization with at least one full time equivalent employee.

(g) "Claim" means a request for payment by a Surety made to a Corporation because of Surety's Loss under a Bond or ILOC secured by a Guarantee, pursuant to section 5010 or 5015.

(h) "Collateral" means those personal and business assets of the Borrower or Principal and guarantor subject to a lien under the Loan or Bond.

(i) "Collection Guarantee" means a guarantee of a specified percentage of the outstanding Loan principal and (ii) ninety (90) days of interest, reduced by any proceeds of the Lender's Liquidation of Collateral as required under Section 5004. A Collection Guarantee will be paid to the Lender only after the Lender has liquidated or made all reasonable efforts in good faith to liquidate all Collateral as required under Section 5004. The total payment made to a Lender under a Collection Guarantee will be the difference between (i) the specified percentage of Loan principal outstanding and ninety (90) days accrued and unpaid interest on the same percentage of the Loan as the Guarantee, and (2) all cash proceeds generated by the Lender in connection with its Liquidation activities required under Section 5004.

(j) "Corporation" means any nonprofit California small business financial development corporation created pursuant to this chapter, or pursuant to Chapter 1 (commencing with Section 32000) of Division 15.5 of the Financial Code.

(k) "Corporate Contract" means a contract executed exclusively between IBank and any individual Corporation.

(l) "Default" means either a delinquency which has not been cured within ninety (90) days, or that the Borrower is in bankruptcy.

(m) "Delinquency" means the failure of the Borrower to make any payment when due, pursuant to the terms of the Loan, except for any principal payment due at the maturity of the Loan.

(n) "Demand" means a request for payment by a Lender to a Corporation pursuant to section 5003 or by a Surety to a Corporation pursuant to section 5015.

(o) "Encumbrance" means a Corporation's outstanding Guarantee balance plus the Farm Loan balance on all Guarantees and Farm Loans in effect. The Guarantee effective date is the date of the executed Guarantee agreement.

(1) The Guarantee balance is calculated as follows:

(A) For a Term Loan, the Guarantee balance is calculated as the outstanding loan balance times the Guarantee percentage.

(B) For a Line of Credit Loan, the Guarantee balance is calculated as the amount of the line times the Guarantee percentage.

(2) The Farm Loan balance is calculated as 40% of the outstanding Loan balance loaned from a trust fund account for the purpose of Farm Loans.

(p) "Farm Enterprise" means the business of producing crops, livestock products and aquatic organisms through the utilization and management of land, water, labor, capital, and basic raw materials including seed, feed, fertilizer, and fuel.

(q) "Farm Loan" means a loan as defined in section 5110(g).

(r) "Full Time Equivalent" (FTE) means the number of full time, part time or other basis employees of a business and its affiliates, in which the employee wages are paid directly from the business.

(s) "Guarantee" means a written agreement to warrant the repayment of a portion of a Loan or payment of all or a portion of a Claim, with repayment from the Corporation's trust fund account. Every Guarantee of a Loan shall be either a Collection Guarantee or Loan Guarantee.

(t) "Goals" means the number of Loans a Corporation expects to Guarantee and the number of Farm Loans a Corporation expects to make during a specified period of time. A Corporation's Goals shall be specified in the Corporate Contract and shall be used by IBank to establish the maximum amount of Expansion Fund moneys to be allocated to a Corporation.

(u) "Holder" means the person or entity purchasing up to eighty percent (80%) of the Loan.

(v) "IBank" means the California Infrastructure and Economic Development Bank.

(w) "ILOC" means an irrevocable letter of credit issued by a Corporation as Collateral for a Bond and which complies with the requirements set forth in section 5014.

(x) "Law" means the Small Business Financial Assistance Act of 2013 (California Government Code 63088 and following and California Corporations Code sections 14000 and following).

(y) "Lender" means a banking organization, including national banks and trust companies and state chartered commercial banks, savings and loan associations, credit unions, state insurance companies, mutual insurance companies, certified community development financial institutions, microbusiness lender and other banking, lending, retirement, and insurance organizations, authorized to conduct business in California.

(z) "Leverage" means the calculation where the numerator is the Encumbrance and the denominator is the Corporation's trust fund account balance.

(aa) "Line of Credit Loan" means a Loan, structured as interest only, for a term not to exceed seven years, except for a Farm Enterprise Loan which shall have a term not to exceed two years, where the minimum repayment is structured as interest only during the term of the loan.

(bb) "Loan" means a Loan or supplier credit extended by a Lender to a Borrower, which is guaranteed pursuant to section 5002, and which is a Term Loan, a Micro Loan, a Line of Credit Loan, or a Revolver Loan.

(cc) "Loan Guarantee" means a Guarantee of a specified percentage of Loan principal and ninety (90) days interest at the same percentage.

(dd) "Loss" means any net monetary damages incurred by a Surety arising out of a Claim, or in pursuing the Surety's rights under the indemnity agreement. As used in this subsection, "net monetary damages" means loss payments, completion costs, reasonable attorney's fees, and reasonable out of pocket consultant fees, costs, and expenses, minus amounts recovered by the Surety from any source, including Collateral. The determination of such loss will take into account amounts recovered, but excluding reinsurance. As used herein, "indemnity agreement" means the written agreement whereby Principal agrees to reimburse Surety for any Loss.

(ee) "Master Agreement" means a contract executed between IBank and one or more Corporations to implement the operating provisions of any of the programs established under the Law.

(ff) "Micro Loan" means a Term Loan not to exceed twenty-five thousand dollars.

(gg) "Multi-party Contract" means a contract executed between IBank and one or more Corporations for the payment of a fee to the Corporations for completing Loan Guarantees and Farm Loans in excess of the Goals described in each Corporation's Corporate Contract.

(hh) "Principal" means an eligible business which has received a commitment for a Bond. In order to be an eligible business, the business must be a "Small Business" as defined in part 121 of chapter 1 of title 13 of the Code of Federal Regulations, as amended

(ii) "Proposal" means a written application to become a Corporation submitted to IBank, and containing the information set forth in the Law.

(jj) "Proposer" means the persons or entity submitting a Proposal to IBank.

(kk) "Remedial Action Plan" means a written set of specifications, with corresponding dates, time frame, designed to correct the problems which resulted in the Suspension Notice or Withdrawal Notice to a Corporation.

(ll) "Revolver Loan" means a Line of Credit Loan which converts to a Term Loan after one year.

(mm) "Surety" means an insurance company licensed by the California Department of Insurance, and authorized to conduct business in California.

(oo) "Suspension" means that a Corporation is no longer registered with the Secretary of State as a small business development corporation and shall not enjoy any of the benefits of a small business development corporation.

(pp) "Temporary Withdrawal" means a limited term suspension of a Corporation's powers to execute Guarantees as long as the Temporary Withdrawal is in effect.

(qq) "Term Loan" means a Loan with regularly scheduled reductions in principal balance.

§ 5001. Guarantee Procedures.

The potential Borrower applying for a Guarantee shall provide a completed Application to the Corporation for review and processing in accordance with the following procedures:

(a) No Guarantee shall be executed by a Corporation until the proposed Guarantee has been reviewed by the Corporation's loan committee and approved by its Board of Directors, unless the Corporation's Board of Directors has delegated the authority to approve a proposed Guarantee to the Corporation's loan committee. No Guarantee shall be approved or executed by a Corporation if the Lender is the same entity as the Corporation issuing the Guarantee.

(b) Upon completion of the review and approval by the Corporation's loan committee and/or Board of Directors, the Corporation shall issue a commitment to Guarantee and an executed Guarantee to the Lender.

(c) In the event that a Guarantee is issued to a Lender without first complying with the requirements of subsection (a), and the Lender relies upon the Guarantee in making the Loan, the failure by the Corporation to so comply shall not constitute a defense on the part of either IBank or the Corporation to paying a Demand for payment made pursuant to section 5003.

(d) In any case where funds are disbursed to a Lender pursuant to a Demand and the Corporation has failed to comply with subsection (a), IBank shall immediately exercise all available legal remedies to recover from the Corporation the funds disbursed pursuant to the Demand.

§ 5002. Guarantee Terms.

(a) Following adoption of a resolution by its board of directors, a Corporation shall be authorized to issue a commitment letter specifying the conditions under which it will issue a Guarantee to a specified Borrower.

(b) The terms and conditions of a Guarantee shall be consistent with the resolution of the Corporation approving the Guarantee and shall include all of the following:

(1) Provision that the Corporation promises to pay up to eighty percent (80%) of the outstanding principal, and accrued yet unpaid interest up to 90 days, on a Loan in which the Guarantee is approved by IBank's Program Manager, subject to the following restrictions:

(A) The Lender has complied with all material conditions contained in the Guarantee, including perfecting Collateral; and

(B) The Lender has not engaged, and will not engage, in fraudulent or negligent practices in connection with the Borrower, Guarantee, the Loan or the Loan Agreement.

(2) The duration of a Guarantee shall not exceed seven (7) years, except for a Line of Credit Loan to a Farm Enterprise, where the duration of a Guarantee shall not exceed two years.

(3) A Corporation does not have the authority to waive a fee or charge more or less than the amount determined and written in the Corporate Contract. The Corporation will not charge an annual servicing fee on loan guarantees. The Corporation shall be authorized to charge the following Loan Guarantee fees as stipulated in its Corporate Contract:

(A) A Loan Guarantee documentation fee of \$250.00.

(B) A Loan Guarantee fee not to exceed 3 percent of the principal amount guaranteed. The Executive Director will set the fee percentage at the time of the Corporate Contract execution and may not change the fee percentage more than twice in each fiscal year.

(4) A statement that the Lender shall send to the Corporation executing the Guarantee, a copy of all Delinquency notices mailed to the Borrower.

(5) A description of the procedures and the responsibilities of the Lender and Corporation subsequent to Default.

(6) Section 5003 Demand procedures.

(7) Agreement to abide by binding arbitration by the American Arbitration Association in the event that either the Corporation or IBank denies the requested Demand pursuant to section 5003(d)(2) or (e)(2), or the amount paid to the Lender is less than the amount contained in the Demand Letter.

(8) Acknowledgment by the Lender that in the event of a Demand, the Lender will allow a bank examiner at the California Department of Business Oversight, or other independent auditor selected by the Corporation, to examine the Lender's Loan files.

(9) A designation as to whether the Guarantee is a Collection Guarantee or Loan Guarantee.

(10) A statement that the maximum amount of interest to be paid is accrued and unpaid, not to exceed ninety (90) calendar days at the guaranteed percentage.

(11) The maximum Guarantee amount for any business is \$2,500,000.00. The maximum Loan amount for any business is \$20,000,000.00, unless specific written approval is obtained from the Executive Director for a larger loan amount.

(12) The small business receiving the loan guaranteed under the SBLGP, a direct loan, or a bond guarantee, must create or retain at least one Full Time Equivalent (FTE) employee as a result of the Loan. This minimal Directive and Requirement is in lieu of a preferred ratio guideline since IBank encourages program participation of single owner operator businesses.

(13) The owner(s) of the business receiving a Loan guaranteed under the SBLGP, a direct loan, or a bond guarantee, shall have at least \$1.00 of equity interest in the business at the time of the Loan. This minimal Directive and Requirement is intended to promote those businesses that may be under-capitalized yet have been deemed credit worthy, due to its other attributes, by a Lender.

§ 5003. Demand Procedures.

(a) The Lender shall be authorized to make a Demand upon the Corporation executing the Guarantee for repayment of the unpaid Loan principal and interest pursuant to the terms of the Guarantee, upon compliance with the following:

(1) Providing proof to the Corporation that the Borrower is in Default and Lender has delivered to both the Borrower and the Corporation a minimum of two letters

subsequent to the Delinquency, at least thirty (30) days apart, explaining the consequences for failure to remedy the Delinquency. This requirement shall not apply if Borrower is in bankruptcy.

(2) If the Guarantee is a Collection Guarantee, providing proof that the Borrower has complied with the liquidation requirements of section 5004.

(b) The Lender shall deliver to the Corporation executing the Guarantee a Demand Letter requesting immediate payment of the guaranteed portion of the allowable accrued and unpaid Loan interest and outstanding principal, and documenting compliance with subsection (a).

(c) Within five (5) days of receipt of the Demand letter, the Corporation shall contract with the California Department of Business Oversight or an independent auditor to conduct an investigation to determine whether the Lender has complied with the terms of the Guarantee, and to issue a report to both the Corporation and IBank. The report shall describe the findings of the investigation for each of the following issues:

(1) Whether the Loan agreement between the Borrower and Lender is consistent with the terms and conditions in the Guarantee.

(2) Whether all Collateral for the Loan and Guarantee have been perfected and maintained.

(3) Whether all Collateral is available for assignment to the Corporation in the event that payment is made upon the Demand.

(4) Whether any Collateral is not available as a result of Lender's negligence, breach of contract, foreclosure or other cause.

(5) If the Guarantee is a Collection Guarantee, whether the Lender has complied with the liquidation procedures of section 5004?

(6) Calculation on the outstanding principal and interest owed.

(7) Whether the Lender complied with the procedures for making a Demand under section 5003(b).

(8) In a section entitled "Loan Information" the report shall include the following information obtained solely from a review of Lender files: a description of the Borrower's business, a description of the Collateral for the Loan, and a discussion as to whether the Lender files contain any reference to matters material to Borrower's compliance with any environmental laws or regulations. The description of Collateral shall identify all real property Collateral as one or more of the following: industrial, commercial, agricultural, single family residence, multi-unit residential, vacant lot, unknown.

(9) A history of loan payments and collection efforts.

(d) Within five (5) days of receiving the California Department of Business Oversight or independent auditor's report, the Corporation shall do one of the following:

(1) Deliver to IBank a request for payment on the Demand, along with: a copy of the report described in subsection (c), the Demand, and a calculation of the amount owed pursuant to the Guarantee; or

(2) Deliver to the Lender, with a copy simultaneously delivered to IBank, a refusal to make payment pursuant to the Demand, and detailing the reasons for refusal.

(e) Within ten (10) business days from the date IBank receives the request for payment on the Demand and a copy of the report described in subsection (c), IBank shall do one of the following and inform the Lender of such action:

(1) Deliver or cause to be delivered to the Corporation a check in an amount not to exceed the amount contained in the Demand Letter, made payable to the Lender; or

(2) Deliver or cause to be delivered to the Corporation a denial of the request for payment to the Corporation based upon noncompliance with the requirements of applicable law, regulations, rules or guidelines, these Directives and Requirements or fraud or negligence on the part of the Lender.

(3) Deliver or cause to be delivered to the Corporation a statement that the investigation or report was incomplete, and requiring the Corporation to complete the investigation and report and resubmit the request for payment to IBank within five (5) calendar days from the date the statement is received by the Corporation.

(f) The amount paid to the Lender pursuant to a Demand Letter shall be less than the amount contained in the Demand Letter only under the following circumstances:

(1) The Demand contains an incorrect calculation of the amount owing;

(2) The amount owing on the Loan has been reduced by subsequent payments from the Borrower to the Lender;

(3) The Lender has engaged in fraudulent activities pertaining to the Loan; or

(4) The Loan and/or the Guarantee is not in compliance with the requirements of applicable law, regulations, rules or guidelines or these Directives and Requirements; or

(5) The report identifies fraud or negligence on the part of the Lender

(g) Within one business day of receiving the check from or on behalf of IBank, the Corporation shall contact the Lender and arrange to deliver the check to the Lender. The Corporation shall deliver the check and simultaneously collect an assignment by the Lender of the Lender's interest in the Loan. The assignment shall include the Loan Note and all Collateral, except as provided in section 5004.

(h) The Guarantee shall include a provision for binding arbitration in the event that either the Corporation or IBank denies the requested Demand pursuant to subsections (d)(2) or (e)(2), or the amount paid to the Lender is less than the amount contained in the Demand Letter.

(i) Demand must be made upon the Corporation no later than noon on the thirty-first calendar day following the date on which the Guarantee terminates; provided, however, that if the thirty-first day is not a day upon which the Corporation is open for business, the last day for making a Demand shall occur on the next succeeding day upon which the Corporation is open for business.

§ 5004. Collection Requirements for Collection Guarantees.

(a) A Lender shall not be authorized to file a Demand for a Collection Guarantee unless it has complied with this section. The requirements contained in this section are in addition to the requirements contained in section 5003.

(b) The Lender must liquidate all Collateral, but shall not be required to file a lawsuit against any Borrower or guarantor. "Liquidate" as used in this paragraph means that the Lender has exhausted all Collateral by one of the following methods:

(1) converted the Collateral into cash;

(2) demonstrated, to the satisfaction of the Corporation that the Collateral is without sufficient value to convert to cash; or

(3) demonstrated that the Borrower has filed for bankruptcy.

§ 5005. Corporation Requirements

The following Directives and Requirements are in addition to Corporation requirements of Corporations Code section 14000 and following, and the Small Business Financial Assistance Act of 2013:

1. A Corporation in existence less than 5 years shall adhere to the same Laws and Directives and Requirements as Corporations in existence for more than 5 years except for a probationary period as indicated in Corporations Code Section 14012.

(a) A Corporation is to maintain a default rate of less than 5% of all of its outstanding guarantees.

- (b) A Corporation must enroll at least one federally supported guarantee, or in the absence of federal funds under the program, one state fund supported guarantee per fiscal year.
- (c) A Corporation must provide all documents related to the Small Business Finance Center programs that are requested from time to time by the Executive Director by the deadline specified by the Executive Director.

§ 5006. Additional Clarifications

- (a) The return on funds from investments may be used for program purposes, including administrative expenses of the Bank and/or the Corporations, at the Executive Director's discretion.
- (b) The Program Manager may create a trust fund account to be shared by multiple Corporations (pooled account) for program uses. The designation of an individual trust fund or a shared trust fund account will be determined by the Program Manager and written in the contract.
- (c) In the event of suspension or termination of a corporation the funds of a Corporation's trust fund account may be transferred to reside in the expansion fund. Use of the principal on the funds shall be governed by the same use of funds in Government Code section 63089.5(b). Since it is the intent to pool the trust fund, it is unlikely a Corporation's trust fund would reside in the expansion fund. If this were to occur, the fund would be used for previously established purposes.
- (d) Corporations shall adhere to the State Small Business Credit Initiative (SSBCI) rules and guidance when supporting a guarantee with SSBCI federal funds. The rules and guidance include, but are not limited to the following resources; the Small Business Jobs Act of 2010, the California Allocation Agreement, SSBCI Policy Guidance, National Standards for Compliance and Oversight, and the SSBCI F.A.Q's.
- (e) The following attachments are the Directives and Requirements for the respective subject areas that are being preserved in their current state, yet may be supplemented, amended or modified in the future.

Attachment A: Surety Bond Guarantees

Attachment B: Secondary Market for Guaranteed Portion of Loans

Attachment C: Farm Loans

