

**CALIFORNIA POLLUTION CONTROL FINANCING AUTHORITY
CALIFORNIA CAPITAL ACCESS PROGRAM (CalCAP)**

Meeting Date: July 15, 2014

***Consideration and Approval of the Collateral Support Program Updates Funded by the State
Small Business Credit Initiative***

Prepared by: *Emily Jarrett*

Summary. On February 17, 2011, CPCFA was awarded approximately \$84 million in State Small Business Credit Initiative (SSBCI) funds by the U.S. Department of the Treasury (Treasury) to fund programs that help small businesses obtain capital. At the time of the award, only CPCFA's CalCAP was utilizing these funds as an approved participating State program. In March 2012, CPCFA requested Treasury's approval to include a Collateral Support Program (CalCAP CS or the Program) to utilize a portion of the allotted SSBCI funds.

In May 2012, staff obtained CPCFA board approval to begin administering the Collateral Support Program upon Treasury's approval. Subsequent to the May board meeting, CalCAP staff actively solicited stakeholder input on the CalCAP CS Program Summary. As a result of Treasury and stakeholder input, CalCAP staff requested and obtained board approval for various refinements to CalCAP CS in December 2012.

Treasury approved the launch of CalCAP CS effective January 17, 2013 and staff launched the Program statewide on January 28, 2013. Additional stakeholder input, as well as CalCAP CS staff experience enrolling loans, necessitated some additional refinements to the Program approved by the board in June 2013. Since June 2013, CalCAP CS has experienced increased participation and, at the current rate, could exhaust the SSBCI allocation in less than one year.

Staff is requesting the changes described in this item to temper the accelerated expenditure of SSBCI funds to ensure CalCAP CS longevity, while maintaining the program's attraction to lenders and borrowers. Such enhancements would transform CalCAP CS into a long term program, guaranteeing a lasting resource and benefit for California's small business lending community.

Background. The SSBCI funds awarded to California totaled approximately \$168 million and are split evenly between CPCFA and California Infrastructure and Economic Development Bank (I-Bank). The funds have been approved to facilitate CPCFA's Capital Access Program (CalCAP) and I-Bank's Small Business Loan Guarantee Program. CPCFA received an initial disbursement of \$27.8 million, which is the first of three "tranches" of its share of the award. CPCFA's second tranche of SSBCI funds totaling \$27.8 million was received in December 2013 and is being swiftly consumed by CalCAP CS.

Description of Proposed Program Updates. Staff proposes the following modifications to the CalCAP CS:

- CalCAP CS would continue to provide up to 40% coverage in the form of a cash deposit on:
 - green and manufacturing loans, and

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- qualified small business loans between \$50,000 and \$250,000.
- For small business loans greater than \$250,000, CalCAP CS would provide up to 30% coverage, reduced from 40%.
- An additional 10% coverage will still be provided for loans where the borrower's business is located in a Severely Affected Community (SAC).
- The minimum loan amount would be reduced to \$50,000 from \$100,000. The maximum would remain at \$20,000,000.
- The maximum collateral deposit of \$5,000,000 will be reduced to either \$2,500,000 for green and manufacturing loans, or \$500,000 for other small business loans.
- The maximum term of support would be 48 months, reduced from 84 months, and the Incremental Recapture Schedule would be modified accordingly.
- CalCAP CS would be modified to allow the renewal of term loans and lines of credit with a maximum collateral support of four years.
- A fee is charged at closing based on the support amount minus the Severely Affected Community portion. The minimum fee would be reduced to \$500 from \$1,000. A 1% fee will be charged for annual renewals on lines of credit.
- No changes are proposed for the implementation of the program. Currently, the exact amount of collateral support for each loan is requested by the lender along with their collateral assessment of the borrower. The final determination of the support amount is at the discretion of the CPCFA Executive Director. The collateral support is pledged, in the form of cash, to cover the collateral shortfall of a loan in order to enable financing that might otherwise be unavailable. This cash collateral is held at the lending institution where the loan is issued or CPCFA's trustee bank, at the Executive Director's discretion. The funds are held in an interest bearing demand deposit account, owned by CPCFA, specific to each loan. The interest accrued in each collateral support account is the property of CPCFA and swept on a periodic basis. The returned support funds will be recycled back into CPCFA to be used for support on future loans. The lender may request a reduction in support at its discretion if it determines that the current level of support is no longer necessary.

Justification for Proposed Program Updates. During this development phase of the Collateral Support Program, CalCAP staff solicited feedback from a variety of lending institutions, including Pacific Enterprise Bank, Manufacturer's Bank, Farmers and Merchants of Central California, and Valley Small Business Development Corporation. These lenders offered differing perspectives and clear input on how to ensure the longevity of CalCAP CS while maintaining the Program's benefits and unmatched flexibility.

This section provides the rationale for each of the proposed updates to CalCAP CS. If approved, the Collateral Support Program Summary will be revised accordingly and published on the Authority's website for lenders who are interested in the using the Program.

Revised Minimums, Maximums, and Contribution Rates. In establishing a balanced pare-down of CalCAP CS, reductions will be made to all aspects of the Program. These reductions were influenced by lender input as well as projection based data using the Program's current portfolio. The new proposed parameters are outlined in the Table A.

| Table A | | | |
|--|---|---|-----------------------------|
| Loan Type | Max. Collateral Support Contribution (per loan and borrower) | Support Rate | Max. Term of Support |
| Green and Manufacturing Loans \$50,000 to \$20,000,000 | \$2,500,000 | Up to 40% of the loan value + 10% for business located in SAC | 4 Years |
| Other Small Business Loans >\$250,000 to \$20,000,000 | \$500,000 | Up to 30% of the loan value + 10% for business located in SAC | 3 Years |
| | | Up to 20% of the loan value + 10% for business located in SAC | 4 Years |
| Other Small Business Loans \$50,000 to \$250,000 | *borrowers who have multiple supported loans may not exceed \$500,000 in total collateral support | Up to 40% of the loan value + 10% for business located in SAC | 4 Years |

Green and Manufacturing Loans. In its first 18 months, CalCAP CS has supported a small number of green and manufacturing loans in California. These transactions have proven costly, time consuming, and risky to the borrower and lender. However, these projects not only create more jobs than the average loan enrolled in the Program, but they also promote California’s greater policy objectives for a sustainable future. CalCAP CS can encourage these worthy projects by providing a higher level of support on eligible transactions. Loans meeting one of the following criteria would qualify for maximum support from CalCAP CS:

1. Loans to be used primarily for supporting new or expanded business processes, products, services, and tenant improvements consistent with specific state policy goals or regulations furthering energy and water conservation, alternative energy and environmental protection.
2. Loans to provide working capital to contractors and other businesses providing specific services furthering energy and water conservation, alternative energy and environmental protection.
3. Loans to be used primarily for new or expanded production of materials and products for use or sale using labor and machines, tools, chemical and biological processing, assembly or formulation.

Fees and Renewals. Under the original design of the Program, lenders were unable to retain the full collateral support on a revolving line of credit. Allowing renewals for lines of credit with a modest 1% fee (minimum \$500) would add the requested flexibility to the Program while encouraging the recapture of the support and preventing overreliance on the funds. The minimum fee for all enrollments will reduce to \$500 to encourage smaller loans and shorter terms of support.

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Loans \$250,000 and Under. CalCAP and CalCAP CS have achieved great success in helping small businesses secure financing. Honoring this spirit and recognizing the risk associated with small loans, transactions \$250,000 and smaller will be eligible for a maximum support of 40% plus 10% for businesses located in SAC. In addition, the minimum loan amount will be reduced to \$50,000 to encourage lending to these small projects that often have the most difficulty obtaining financing.

Maximum Term of Support. To sustain this program, staff recommends reducing the maximum term of support from 7 years to 4 years, and adjusting the Incremental Recapture Schedule accordingly. This modification will provide the most benefit of the cash deposit to the lender and borrower when the outstanding principal balance on a loan remains the highest, and returns the funds to CPCFA in a timely fashion to sustain the program.

Staff Recommendation. Staff recommends the approval of these updates to CalCAP CS, consistent with SSBCI standards and CPCFA statute, in order to ensure CalCAP CS is a long term resources for business seeking capital

**RESOLUTION OF THE CALIFORNIA POLLUTION CONTROL
FINANCING AUTHORITY APPROVING UPDATES TO THE
COLLATERAL SUPPORT PROGRAM**

July 15, 2014

WHEREAS, the California Pollution Control Financing Authority (“Authority”) was created under the provisions of Section 44500 of the Health and Safety Code; and

WHEREAS, Article 8 (commencing with Section 44559) of Chapter 1 of Division 27 of the Health and Safety Code provides that the Authority is authorized to establish a Capital Access Program for Small Businesses (“CalCAP”); and

WHEREAS, Section 44519 of the Health and Safety Code provides that the Authority may employ an Executive Director and any other persons as are necessary to enable it to properly perform the duties imposed upon it by the Authority’s statutes; and

WHEREAS, the Authority received an award from the United States Treasury (“Treasury”) under the federal State Small Business Credit Initiative (“SSBCI”) to further the objectives of the Authority’s CalCAP, and for a Collateral Support Program funded by the SSBCI award; and

WHEREAS, the Authority has determined that specific revisions to the Collateral Support Program (as more fully described in the July 15, 2014 staff report to the Authority) are necessary for the successful implementation of the Program.

NOW, THEREFORE, BE IT RESOLVED by the California Pollution Control Financing Authority as follows:

Section 1. The proposed Program presented at the July 15, 2014, meeting is hereby approved in substantially the form submitted. The Chair, Executive Director, or Deputy Executive Director is hereby authorized, for and on behalf of the Authority, to proceed with the approved updates to the Collateral Support Program.

Section 2. The Chair, Executive Director, or Deputy Executive Director of the Authority are hereby authorized and directed to take such actions to implement these approved updates, make such changes to the Collateral Support Program as may be required by Treasury under the terms of the SSBCI award, make or cause to be made such changes to the Regulations as may be required, and to execute and deliver any and all documents that they may deem necessary or advisable in order to effectuate the purposes of this Resolution

Section 3. This Resolution shall take effect immediately upon its approval.

Attachment A

California Pollution Control Financing Authority

CalCAP Collateral Support

CalCAP Collateral Support (CalCAP CS) encourages banks and other financial institutions to make loans to small businesses that have difficulty obtaining financing. CalCAP CS pledges cash to cover the collateral shortfall of a loan in order to enable financing that otherwise might not be available to a small business.

Eligible Uses of Loan Proceeds

Loans can be used to finance green businesses and projects, manufacturing, the construction or renovation of buildings, the purchase of equipment, other capital projects, working capital, and bridge loans needed prior to obtaining permanent financing (including SBA 504 bridge loans). There are limitations on loan refinancing.

Ineligible Uses of Loan Proceeds

CalCAP CS prohibits financing of passive real estate, residential real estate, business acquisitions, any portion of a SBA loan, and those uses prohibited by the State Small Business Credit Initiative [guidelines](#).

Eligible Small Businesses

An eligible borrower must be in one of the industries listed in the [North American Industry Classification System \(NAICS\)](#) codes list, must not be prohibited by the State Small Business Credit Initiative [guidelines](#), and have fewer than 750 employees. The borrower must have their “Primary Economic Effect” in California where one of the following conditions exists: at least 51% of the total revenues of the business activity are generated in California; or at least 51% of the total jobs of the business are created or retained in California.

Green and Manufacturing Loans

Loans meeting one of the following criteria would qualify for maximum support from CalCAP CS:

1. Loans to be used primarily for supporting new or expanded business processes, products, services, and tenant improvements consistent with specific state policy goals or regulations furthering energy and water conservation, alternative energy and environmental protection.
2. Loans to provide working capital to contractors and other businesses providing specific services furthering energy and water conservation, alternative energy and environmental protection.
3. Loans to be used primarily for new or expanded production of materials and products for use or sale using labor and machines, tools, chemical and biological processing, assembly or formulation.

Attachment A

Terms of Support

CalCAP CS provides up to 40% coverage in the form of a cash deposit on eligible green and manufacturing loans and qualified small business loans between \$50,000 and \$250,000. For small business loans greater than \$250,000, CalCAP CS provides up to 30% coverage. An additional 10% coverage will still be provided for loans where the borrower’s business is located in a Severely Affected Community (SAC). The minimum loan amount is \$50,000 and the maximum loan amount is \$20,000,000. The maximum support amount for eligible green and manufacturing loans is \$2,500,000 per borrower and per loan, or \$500,000 for other small business loans. Table A outlines the parameters of the Program.

TABLE A

| Loan Type | Max. Collateral Support Contribution (per loan and borrower) | Support Rate | Max. Term of Support |
|--|--|---|----------------------|
| Green and Manufacturing Loans \$50,000 to \$20,000,000 | \$2,500,000 | Up to 40% of the loan value + 10% for business located in SAC | 4 Years |
| Other Small Business Loans >\$250,000 to \$20,000,000 | \$500,000 *borrowers who have multiple supported loans may not exceed \$500,000 in total collateral support | Up to 30% of the loan value + 10% for business located in SAC | 3 Years |
| | | Up to 20% of the loan value + 10% for business located in SAC | 4 Years |
| Other Small Business Loans \$50,000 to \$250,000 | | Up to 40% of the loan value + 10% for business located in SAC | 4 Years |

Lenders set all the terms and conditions of the loans. Loans can be short- or long-term, have fixed or variable rates, and bear any type of amortization schedule. The term of the support will be at the lender’s discretion, not to exceed the original term of the loan or 4 years, whichever is less. Lenders are free to determine the amount of collateral support they wish to request and may also choose to reduce the collateral coverage at any time for any reason.

Eligible Lenders

Any federal or state-chartered bank, savings association, federally certified Community Development Financial Institution (CDFI), or credit union is eligible to participate in CalCAP CS. A lender must certify that it is in good standing with its regulatory body (Federal Reserve, Federal Deposit Insurance Corporation (FDIC), Comptroller of Currency, Thrift Supervision, National Credit Union Administration (NCUA), or state banking authority). Existing CalCAP lenders, who meet the above requirements, are already eligible to participate in CalCAP CS.

A Qualified Lender must sign the [Certification to Participate in Federal Fund](#) to participate in any Federally funded program and is required to abide by the assurances.

To become a participating lender in the CalCAP CS, submit [Financial Institution Application](#) and [Certification to Participate in Federal Fund](#) to CalCAP@treasurer.ca.gov.

How to Request Collateral Support for a Loan

Prior to the issuance of a loan, a lender must submit a [Collateral Support Request](#) and a risk assessment of the borrower. The risk assessment includes: the value of the collateral based on the industry standard

Attachment A

of measurement (e.g. appraisal); the lender’s valuation of the collateral including the need for collateral support; borrower’s risk rating; summary of relationship and history of the business; and the lender’s cash flow and financial analysis of the borrower. Once the request has been approved by the CPCFA Executive Director, a Collateral Support Approval will be sent to the lender. This commitment can be called upon for up to 90 business days after issuance. The Collateral Support Approval will include instruction from CalCAP CS that a loss reserve account be opened when the loan is finalized. This collateral support loss reserve account is owned by CPCFA. A separate account will need to be opened for each loan that is enrolled in the Program.

Within 15 business days of the closing of the loan, the lender will submit the Collateral Support Approval with the final loan information and closing fees assessed according to Table B, notifying CalCAP CS that the loan has been funded. The SSBCI [Lender Certification](#) and [Borrower Certification](#) must be signed and submitted with the final loan information. The lender is required to give the borrower a [Privacy Notice](#). The final loan information must be accompanied by evidence the collateral support loss reserve account has been opened and applicable fees deposited. In turn, CalCAP CS’s trustee bank will wire the cash collateral support amount into the bank’s loss reserve account for each loan. The lender is required to provide a confirmation of receipt of funds.

Collateral Support Loan Loss Reserve Account

The Collateral Support Loan Loss Reserve Accounts are Interest Bearing Demand Deposit Accounts, owned by CPCFA, generally held at the lending institution, and specific to each loan. Non-depository financial institutions’ loan loss reserve account will be held at CalCAP CS’s trustee bank. In addition, the CPCFA Executive Director may require any account be held at the trustee bank.

The collateral support for each loan will be reduced annually according to the Incremental Recapture Schedule (Table C). The lender can also request a reduction in support at their discretion if they determine that the current level of support is no longer necessary.

The interest earned on the collateral support loss reserve account is the property of CPCFA and will be periodically swept.

Fees

TABLE B

| Original Term Support of | Eligible Green and Manufacturing Loans | Bridge Loans | Small Business Loans |
|---------------------------------|---|---------------------|-----------------------------|
| ≤ 12 months | 0.50% | 0.50% | 0.50% |
| 12.1 months - 24 months | 0.75% | 0.50% | 0.75% |
| 24.1 months - 36 months | 2.00% | 2.00% | 2.00% |
| 36.1 months - 48 months | 2.75% | 2.75% | 2.75% |

A fee is charged at closing on the support amount. There is a minimum fee of \$500 for all loans. Fees will not be charged on the Severely Affected Community portion of the support. For bridge loans, a fee of 0.5% will be charged on the support amount for requested extensions. A 1% fee will be charged for annual renewals on lines of credit, up to a maximum of four years.

Attachment A

Incremental Recapture Schedule

TABLE C

| Original Term of Support | Annual Review | | | |
|--------------------------|---------------|-------|----|---|
| | 1 | 2 | 3 | 4 |
| 0-12 Months | | | | |
| 12.1-24 Months | 50 | | | |
| 24.1-36 Months | 33.33 | 33.33 | | |
| 36.1-48 Months | 25 | 25 | 25 | |

*Inapplicable to bridge loans

-  equal to the percent of the original contribution amount
-  repayment of entire support upon support expiration

On an annual basis, in conjunction with the loan anniversary, a portion of the support will be returned to CPCFA according to the Incremental Recapture Schedule. The portion to be returned will be based on the original term of the support. However, bridge loans will experience the recapture once the balance of the loan is paid off or the related guarantee goes into effect. Any additional reductions requested by the lender will also be taken at this time.

Default and Charge-Off

Lender must submit a [Collateral Support Default Notification](#) upon loan default, or within 30 calendar days after the maturity of the support, in order to freeze further reductions from the support account and additional fees.

Within 30 calendar days of collateral liquidation, the lender will submit a Collateral Support Claim Application, history of the account payments, a short narrative of the loan collection history, and information about the sale of proceeds or justification for failed attempts to liquidate. State's collateral shall not be used in lieu of pledged collateral. All collateral must be liquidated consistent with the participating financial institution's usual method for loans that do not have the State's support. Lenders may be reimbursed for: the amount of loan principal charge-off; reasonable out-of-pocket expenses incurred in pursuing its collection efforts, including the preservation of collateral, and other related costs; and accrued and unpaid interest. Proper documentation of any claimed expenses shall be presented at the time of the claim. The amount paid on a claim will never exceed the available amount in the Collateral Support Loss Reserve account.

If subsequent to the payment of the claim the lender recovers from the borrower by any source, the lender may fully cover their loss and return any excess to CalCAP CS (not to exceed the total amount paid on the claim by CalCAP CS).

Reporting and Records Retention

Lenders are required to send monthly bank statements to CalCAP CS by the 15th of the following month for all collateral support loss reserve accounts. All loan documents associate with loans enrolled in CalCAP CS are required to be retained until January 31, 2020.