EL DORADO COUNTY
BUSINESS LOAN PROGRAM GUIDELINES

I. PURPOSE:

The County of El Dorado Business Loan Program (BLP) is designed to provide the critical and necessary capital needs for business and real estate projects within the County. The BLP will be capitalized with funds from the State of California Community Development Block Grant (CDBG) Program. The intent of the BLP is to provide appropriate assistance to businesses and real estate development projects, which in turn will create and/or retain jobs, along with increasing the commercial and industrial base of the community.

The Business Loan Program provides loans, in which repayments are “revolved” or “recycled” to be loaned again in the same program. Therefore, the initial funds that capitalize the program will be used again to create additional jobs, assist more businesses and projects, and provide significant benefits beyond the Business Loan Program’s initial loans.

The Business Loan Program will assist businesses and projects that start-up, expand, and/or locate within the unincorporated areas of the County. The Business Loan Program proceeds can be used to finance:

- Working Capital/Lines of Credit,
- Inventory Purchase,
- Equipment Acquisition,
- Real Property Acquisition, Construction, Rehabilitation; and
- Furniture/Fixtures.

II. POLICY:

The following elements are critical in the selection of loans for the BLP:

- That the terms and conditions of the Business Loan Program are appropriate;
- That a sufficient number of jobs will be created or retained in accordance with CDBG requirements;
- At least 51% of the jobs created and/or retained must be from the Target Income Group (TIG). The TIG is a low/moderate income person whose household income does not exceed 80% of County median household income, adjusted by family size. In order to meet the criterion for created and/or retained jobs, the employees must be from the TIG at the time they are hired or retained. For job retention projects, income self-certification will be conducted on all employees prior to the approval of the loan. For job creation projects, all of the TIG employees will complete income self-certification; and
- The loan meets the Business Loan Programs underwriting requirements.

Eligible applicants include ongoing and start-up private, for profit business concerns, corporations, partnerships, sole proprietorships and cooperatives that are incorporated and licensed, and are located in or locating to the County. The project to be financed with the Business Loan Program must be within the unincorporated area of the County.

The project must be commercial or industrial. Business Loan Program funds can be used for construction and permanent financing, working capital, inventory equipment, real property acquisition, construction and rehabilitation.

III. SOURCE OF FUNDING

The source of funding for the Business Loan Program is the State of California Community Development Block Grant Enterprise Fund Component Program. Loans are not from the El Dorado County General Fund.

IV. DESCRIPTION OF FUNDING

4.1 Guidelines:

Loans will range from a minimum of $5,000 to a maximum of $100,000. Although all loans must be reviewed by HCD/CDBG prior to final approval, loans above $250,000 will require additional approval by the State Department of Housing and Community Development's (HCD) loan committee.

- **Leveraging**: The Program's overall goal is to leverage a realistic pledge of dollars from equity and/or debt for every one Program dollar loaned. On a case-by-case basis this leverage requirement may be waived. A private dollar can be either debt financing or owner equity. Owner equity can be cash and/or land. The land is counted only for construction projects. Expenditures made by the loan applicant prior to the Business Loan Program loan award are not counted unless made as part of the submittal, and made within 60 days of the Business Loan Program loan submittal, related to and in anticipation of such submittal. **A minimum of 10% of the total project funding must be from owner equity.**
- **Loan Terms**: Up to ten years, depending on the asset being financed, and the demonstrated need for the Business Loan Program funds. The length of loan shall not exceed the economical life of the equipment/asset being financed.
- **Loan Fee**: A loan fee of up to 1.5% may be charged to the borrower.
- **Prepayment Penalty**: None
- **Deferral of Payments**: On a case-by-case basis, determined based on the financial gap.
- **Job Creation and/or Retention**: One full time equivalent job (1,750 hours annually) per $35,000 loaned shall be achieved for each loan. Two permanent part-time jobs (at least 875 annually) can be aggregated to count as one full time equivalent job. For loans meeting the national objective of principally benefiting the Targeted Income Group (TIG), at least 51% of the jobs created/retained shall be held by TIG persons.
- **Collateral Requirements**: All Business Loan Program loans shall be fully secured by collateral in order to maintain the Business Loan Program. No unsecured loans shall be made. Types of collateral may include liens on real property; deeds of trust; liens on machinery, equipment or other fixtures; lease assignments; personal and/or corporate guarantees; and other collateral, as appropriate.

4.2 General Administrative Features:

The Business Loan Program will comply with all CDBG requirements, including, but not limited to:

- Confidentiality of Client Financial Information, as allowed by law;
- Equal Opportunity/Affirmative Action Policy;
- Attorney review all contracts and legal forms;
- Monitoring and Reporting Forms;
- Collection and Foreclosure Policy;
- Labor standards (where applicable);
- Clearing CDBG special conditions;
- Relocation assistance (where applicable);
- Section 3 requirements;

- Fair Housing requirements;
- Environmental reviews; and
- The County staff will be responsible for overall project marketing, loan evaluation, loan packaging, and monitoring.

4.3 Project Evaluation Criteria

The following evaluation criteria will be adhered to during the course of the Business Loan Program:

- The number of jobs created and/or retained and the percentage benefiting members of the targeted income group;
- The amount of private dollars leveraging BLP funds;
- The financial viability of the proposed enterprise; and
- The demonstrated need for the funds.

4.4 General Credit Requirements

Loan Applicant must be:

- Be of good character;
- Show ability to operate a business successfully;
- Have enough borrowing ability or equity to operate, with the loan, on a sound financial basis;
- Show the proposed loan is of sound value or reasonably secure to assure repayment; and
- Show that the past earnings record and future prospects of the firm indicate ability to repay the loan and other fixed debt, if any, out of the profits.

4.5 Loan Packaging

The County staff will be responsible for the loan packaging activities, including review of all proposals presented to the Loan Advisory Board (LAB).

4.6 Loan Advisory Board

The Loan Advisory Board (LAB) shall be responsible for reviewing funding proposals and making recommendations to County staff. The El Dorado County Housing, Community and Economic Development Agency will decide the terms and conditions of loan agreements. The LAB shall be comprised of:

- One representative of County staff; and
- One Certified Public Accountant;
- Two representatives of a El Dorado County lending institution; and
- Two representatives of the business community appointed by the County.

All projects meeting the established criteria shall be brought before the LAB. HCD/CDBG will make the final loan determination after County LAB approval.

4.7 Length of Review Process

On average, the BLP review process takes six to eight weeks from submittal of a complete loan application through LAB review. Loan funds can be disbursed two to three weeks after signing the BLP documents, depending on the financing. All loans must be approved in advance by HCD. Additional commitments can be made prior to final approval from another funding source. Every effort will be made to facilitate the process to coincide with the other funding source and the project's requirements.

4.8 Linking Jobs with Long-Term Unemployed

County staff will work closely with the local One Stop Center to support the Workforce Investment Act (WIA) programs and services that provide assistance to the unemployed and low and moderate-income persons. Early and consistent involvement with each loan applicant will be an integral policy of the BLP.

V. ELIGIBLITY

5.1 Eligible Applicants

Eligible applicants include ongoing and start-up private, for profit business concerns, corporations, partnerships, sole proprietorships and cooperatives that are incorporated and licensed, and are located in or locating to the County. The project to be financed with the BLP must be within the unincorporated area of the County.

5.1.1 Conflict of Interest

When the County's program contains Federal funds, the following shall be addressed: in accordance with title 24, Section 570.611 of the Code of Federal Regulations, no member of the governing body and no official, employee or agent of the local government, nor any other person who exercises policy or decision-making responsibilities (including members of the loan committee and officers, employees, and agents of the loan committee, the administrative agent, contractors and similar agencies) in connection with the planning and implementation of the Program shall directly or indirectly be eligible for this Program. This ineligibility shall continue for one year after an individual's relationship with the County ends. Exceptions to this policy can be made only after public disclosure and formal approval by the governing body of the locality.

5.2 Eligible Uses

The project must be commercial or industrial. BLP funds can be used for construction and permanent financing, working capital, inventory, equipment, real property acquisition, construction and rehabilitation.

5.3 Ineligible Uses

Projects must be located in the unincorporated part of El Dorado County. Projects cannot be residential in nature. Projects must have reasonable assurance of repayment. Projects are not eligible if they create a conflict of interest pursuant to California Government Code S87100 et seq for any current County employee or Loan Advisory Board (LAB) member. Projects must create or retain jobs, primarily for the Targeted Income Group, and must leverage private or equity funds.

5.4 Eligible Projects

Project eligibility is based on the project satisfying the CDBG Program's national objective of principally benefiting targeted income group persons through job creation and/or retention, or aid in the elimination of slums or blight or meet a community development need having a particular urgency. Additionally, the eligibility of a project is dependent on the appropriate determination being made to justify the provision and extent of CDBG assistance.

5.5 Eligible Costs

- Land costs, including engineering, legal, grading, testing, site, mapping and related costs associated with the acquisition and preparation of land.
- Building costs, including real estate, engineering, architectural, legal and related costs associated with acquisition, construction and rehabilitation of buildings including leasehold improvements.
- Working capital, inventory, furniture, fixtures, machinery and equipment.

5.6 Ineligible Costs for CDBG Loans

- Costs incurred prior to CDBG grant execution, submittal of the loan application, and environmental review requirements, except for private leverage as specified in Section 4.1.
- Costs other than those listed as eligible in Section 5.5.

VI. ROLE OF THE COUNTY

6.1 Role of the County Staff

County staff will, as required will:

- Publicize and market the BLP;
- Screen all applicants for loans;
- Meet with potential lenders;
- Perform site visits, as appropriate;
- Refer candidate that are not eligible, do not meet the BLP criteria or need technical assistance to the Small Business Development Center;
- Obtain from candidates preliminary information and an application, along with accompanying financial information;
- Prepare packages, along with recommendation to LAB;
- Perform any appeal process;
- Provide expenditure reports and other miscellaneous information to County to operate the BLP;
- Assist the County in any implementation process of the BLP (clearing special conditions, environmental review, etc.).
- If approved, assist with loan processing and closing; and
- Once closed, monitor the loan, maintain the loan records, and monitor compliance with job objectives.

The County of El Dorado staff is responsible to:

- Provide the overall oversight and liaison among the County Staff, loan applicants, recipients, lenders, and other interested parties;
- Prepare all reports, financial information and performance reports as required by CDBG on each loan during the term of the loan;
- Serve as the contact for the State Department of Housing and Community Development for the BLP;
- Meet with each BLP applicant at the application conference (prior to submission of application to LAB) to review application and ensure the applicant understands all requirements and obligations of the BLP;
- Perform any special conditions clearances required by CDBG;
- Review the standard loan documents (in conjunction with County Legal);
- Amend and submit for approval the BLP guidelines and reuse plan as needed;
- Meet with lenders as appropriate;
- Make the final decisions to foreclose and declare defaults (in consultation with legal counsel, based upon recommendations of staff);
- Monitor on-going operations of the loan recipient;
- Monitor compliance with BLP requirements;

- Attend HCD/CDBG training as appropriate; and
- Assist other County departments as required to implement loan application (Planning/Building, DOTS, etc.).

6.2 Role of the Loan Collection Agent

The County will conduct the duties of loan collection agent. The duties will include the following:

- Loan servicing and accounting;
- Provide monthly receipts of loan payments;
- Provide quarterly statements on each loan;
- In concurrence with the County's legal counsel, undertake loan collections, including asset liquidation; and
- Obtain credit reports on all loan applicants.

VII. LOAN SELECTION AND APPROVAL PROCESS

7.1 (A) Marketing

The marketing of the BLP will be accomplished by a variety of means. There will be media coverage, marketing brochures, and joint marketing through County Staff's existing loan packaging and financial services. Local lenders will recommend clients and projects, when appropriate. The Small Business Development Center, local Realtors, and business associations will also refer potential applicants. The County staff will also use existing business and community networks to market the BLP.

7.1 (B) Procedure

Once a potential project has been identified, the County staff will conduct a preliminary review for eligibility with the BLP criteria. If another lending source is more appropriate, or the project does not meet the BLP criteria, the County staff will refer the prospective borrower to another organization for assistance and technical assistance. This will include referrals to the Greater Sacramento Small Business Development Center, the SCORE program, and financial institutions. As a condition of the loan, the County staff or LAB may require that applicants receive pre-loan and/or post-loan counseling.

County staff may require applicants who have received loans to undertake business counseling if it appears that the applicant's financial position is declining and the BLP loan may become delinquent.

If the project appears to meet the criteria, the applicant will be asked to submit preliminary information. Preparation and submission by an applicant of preliminary information and supporting documents include, but are not limited to:

- Business and personal tax returns for the last three years or since commencement of operations (whichever is less);
- Business financial statements (balance sheet and income statement) for current year and prior three years;
- Current personal financial statement;
- Credit history; and
- A proposed project summary.

Start-up businesses must submit pro-forma financial statements for the first three years. Real estate projects must submit pro form projections for the first five years, and pre-leasing information.

The County staff will review the preliminary information. If the project is viable, a draft loan analysis will be prepared. If the decision is to decline the request, the County staff will provide the applicant with a written explanation of the denial. If appropriate, referrals to other organizations will be made.

If the review is positive, the applicant will be invited to an application conference with County staff and to submit a formal application to County staff, which will be presented to the LAB for their recommendation. At the application conference, the County staff will review with the applicant the formal BLP checklist and required information, forms and financial schedules deemed necessary by County staff to complete the loan package. County staff will determine project needs/conformance with local requirements, including the necessary environmental review for the project.

The applicant, in conjunction with the County staff will develop the employment agreement.

Upon completion of the necessary information, the County staff will present applications to the LAB. The presentation will include a completed BLP Project Evaluation form. If the private funds are from equity, then the commitment letter must be from the applicant. The County staff presentation will include a recommendation. This recommendation will include the proposed terms and conditions, based upon the identified "financial gap" and the appropriate analysis undertaken by County staff, along with a checklist insuring that the loan meets the BLP guidelines and criteria.

The LAB will decide to recommend approval or to decline the loan request. If loan request is declined, the applicant will be informed in writing by County staff as to the reason. If recommended, the LAB's recommendation may be based on the terms and conditions proposed by County staff, or the LAB can recommend alternative terms and conditions. The LAB recommendation is to be presented to the County staff. Prior to final County approval, County staff will review the loan package for completeness and regulatory compliance, as well as final review for compliance with BLP guidelines and criteria.

When the County approves or denies the loan request, the applicant will be notified in writing. If denied, the reasons for denial will be included. The County staff approval shall include a certification statement that, based on his/her review of the staff report and LAB recommendation, the County finds that the CDBG loan is appropriate and that the assistance is commensurate with both the needs of the borrower and level of benefit to TIG persons in addition to other public benefits stemming from the project.

7.1 (C) <u>Loan Closing</u>

Upon approval by County LAB, the County Staff will complete the special conditions (including the environmental review). Once approved by HCD/CDBG the Borrower will sign all the necessary documents and agreements. County staff will request a draw down of funds from the State Department of Housing, Community and Economic Development (the timing of the request may vary depending on the project). The County staff will prepare the loan closing documents, prepare title and lien searches, and UCC-1 filings, if appropriate (the sample pre-closing checklist and escrow instructions attached will be developed and used for each loan closing). County legal counsel will review all agreements and documents, as necessary.

The County staff will undertake loan closing. At the time of closing, the Borrower will be provided with a checklist outlining their obligations under the BLP. At closing, or another specified time, funds will be disbursed to the Borrower.

The County staff will complete any remaining legal, regulatory or other items. Monitoring and compliance files will be set-up at this time.

7.1 (D) Loan Monitoring

Two separate loan files will be maintained. The first is the legal file, which holds all the original loan documentation, along with the original documents. This file shall be kept in the County's fireproof vault for safekeeping. The second is a credit file, which shall contain the day-to-day administrative records of the loan.

The legal file shall include, at a minimum:

- Note;
- Loan Agreement, including Non-Financial Employment Plan;
- Mortgage;
- General Security Agreement;
- Personal Guaranty;
- Corporate Guaranty;
- Subordination Agreement;
- Life Insurance Policy and Assignment;
- Hazard Insurance Policy and Assignment;
- General Resolution;
- Certificate of Secretary;
- Opinion of Counsel; and
- Inter-creditor Agreement.

The credit file shall contain, at a minimum:

- Loan Application;
- Financial Information Associated with the Application;
- Credit Memo;
- LAB Recommendation;
- Final County Approval;
- Disbursement Records;
- Reports of Site Visits;
- Updated Financial Information Provided by Borrower; and
- Job Creation/Retention Data.

A reporting system will be established for each loan and the loan portfolio as a whole. The report should be updated at least quarterly. The County staff shall be responsible for preparation of this report. The County staff will use the report to monitor the loans and identify problems. The report will contain the following:

- **Fund Report Balance:** A monthly summary of the beginning fund balance, principal and interest recaptured during the month, disbursements made during the month and funds committed but not yet disbursed, and amount remaining in the BLP which is unencumbered. The monthly receipts from the lender on each loan will serve as the basis for this report.
- **Portfolio Summary Report:** A quarterly summary of the total loans outstanding and authorized loans. The report shall include a quarterly statement on each loan, prepared by the lender. The quarterly report shall include the last payment date and loan balance. Delinquent loans shall be identified and a summary of actions to date to collect delinquent loans shall be included.
- **Employment Report:** A quarterly report on each project detailing the jobs created/retained, and those hired that meet the Targeted Income Group.
- **Loan Loss and Delinquent File:** A list of all loans that have been classified as uncollectible and a summary of foreclosure procedures to date on the loan. Loans that are delinquent will also be listed, along with a summary of recommended steps, and steps taken to date.

- **Tickler File:** A listing of the current loan portfolio and dates for receipt of financial statements, employment information, renewal of UCC-1 filings, review date, dates for insurance renewal and other information.

In addition, the County staff will establish and maintain a loan monitoring file which will include a summary of the monitoring requirements of the State Department of Housing and Community Development. A tickler file will be part of this overall file to insure that loan and BLP monitoring is undertaken and completed.

VIII. LOAN UNDERWRITING

The loan underwriting policies of the El Dorado County Business Loan Program (BLP) are designed to insure the Program's ongoing viability, assist businesses that could not proceed without the BLP, and ensure that the BLP assistance is appropriate.

8.1 HUD Underwriting Guidelines:

The County has adopted the HUD underwriting guidelines for the BLP to determine whether a proposed CDBG subsidy is appropriate to assist with business expansion or retention. In addition, the project will be reviewed to determine that a minimum level of **public benefit** will be obtained form the expenditure of the CDBG funds in support of the project.

The objectives of the underwriting guidelines are to ensure that:

- Project costs are reasonable;
- All sources of project financing are committed;
- To the extent practicable, BLP funds are not substituted for non-Federal financial support;
- The project is financially feasible;
- To the extent practicable, the return on the owner's equity investment will not be unreasonably high;
- To the extent practicable, BLP funds are disbursed on a pro rata basis with other financing provided to the project; and
- Sufficient public benefit will be received from the expenditure of BLP funds.

8.1(A) Project Costs are Reasonable

All project costs will be reviewed for reasonableness, and to avoid providing either too much or too little BLP assistance. The amount of time and resources expended evaluating the reasonableness of a cost element shall be commensurate with its costs. In some instances, it will be necessary to obtain third-party, fair-market price quotations or a cost element. Particular attention will be documenting the cost elements in non-arms-length transactions.

Procedures:

1. Start with Sources and Uses of Funds.
2. For each Use of funds, determine if costs are reasonable.
    a. For construction, machinery, equipment. Determine if the costs are estimated by a third-party (e.g. architect, engineer, equipment supplier, etc.). Determine if the estimates are included in the application. Determine if the contingency is adequate.
    b. For land, determine if the price is based upon Fair Market Value. If not, determine the Fair Market Value and how was price determined. Obtain an appraisal or an opinion of Fair Market Value.

c. For development costs (building fees, architectural/engineering costs, financing costs, franchise fees, etc.), determine if these costs are itemized and supported by contracts or other documentation.
d. For working capital, compare the amount of working capital to industry averages, risk, historical needs of the business and the projected need. Analyze business financial statements, projections, operating cycle and financial ratios.

3. A higher level of review will be required if there are no third party estimates.
4. Sources of information:
   - Sources and Uses of Funds Statement;
   - Financial Statements and Projections;
   - Industry Averages (Robert Morris):
   - Third Party Costs Estimates;
   - Building Department/Public Works;
   - Realtors;
   - Appraisers;
   - Architects/Engineers;
   - Contractors;
   - Equipment Suppliers; and
   - Other similar projects.

8.1 (B) Commitment of All Sources of Project Financing

Prior to the commitment of BLP funds to the project, a review shall be conducted to determine if sufficient sources of funds have been identified and committed to the project, and the participating parties have the financial capacity to provide the funds to ascertain if the project is viable and will move ahead in a timely manner. In certain circumstances, the BLP may commit its funds in advance of final commitments from other funding sources. However, to conduct the underwriting analysis, the approximate terms and conditions of the other funding sources should be known. Final commitments from the other funding sources will be required, with substantially similar terms and conditions as used in the underwriting analysis, prior to any loan closing or disbursement of funds.

Procedures:

1. Start with Sources and Uses Form.
   a. For all sources of funds, determine if there is evidence verifying commitment or intent to commit.
   b. For debt sources, be in receipt of letters of intent or interest, which specify the level of commitment and terms/conditions of the loan. The proposed terms should be reflected in the business projected debt schedule and in the financial projections. Determine if actual loan packages have been submitted to lenders.
   c. For equity sources, determine if the equity injection is verified on the business or personal financial statements. Or if an investor provides the equity, obtain evidence of the level and terms of commitment (e.g. letter of intent with accompanying financial statement verifying availability of funds).
2. Sources of information:
   a. Sources and Uses of Funds,
   b. Business and Personal Financial Statements, and
   c. Letters of intent/interest form lenders, partners and investors.

8.1 (C) Avoid Substitution of CDBG Funds for Non-Federal Financial Support

The project will be reviewed to ensure that, to the extent practicable, BLP funds will not be used to substantially reduce the amount of non-federal financial support for the project to make the most efficient use of the BLP funds.

8.1 (D) Financial Feasibility of the Project

Each project will be examined to determine the financial viability of the project, and thus the reasonable assurance that the public benefit will be realized. The current and past financial statements for both the business and individuals must be analyzed, along with tax returns and projections. The assumptions behind the projections must be critically analyzed. Income and expense costs shall be evaluated and compared historically, where applicable, and compared to industry averages (using guides such as Robert Morris' Annual Financial Statements). Project costs, including both hard and soft costs, must be determined to be reasonable. Accurate project costs are vital to determining project feasibility.

As part of the financial analysis, the past, current, and projected financial data shall be analyzed to determine if the job estimates are reasonable and supportable. Labor costs shall be looked at the break-even point. In addition, labor costs shall be checked against industry averages. Variations should be explained in the loan analysis.

The terms and conditions of the BLP loan must be appropriate. In general, the interest rate shall be set at a rate where available cash flow is able to meet debt obligations, after other obligations are met, with enough cash flow remaining to operate successfully. The loan term typically is based in the asset being financed. The term should not exceed the economic life of the asset being financed. However, a longer loan amortization schedule, with the loan due at the end of the economic life may be justifiable

Each loan shall include a written explanation of the appropriate analysis that was undertaken, and the reason the terms and conditions of the loan were approved.

8.1 (E) Financial Analysis.

Historical and projected financial statements will be subject to financial analysis to determine the gap, and structure the terms and conditions of the BLP loan, as discussed above, but also to determine that the project is feasible. In addition, use prudent underwriting guidelines, demonstrating that the proposed loan is of sound value, and note how past earnings and future prospects indicate an ability to meet debt obligations out of profit.

Information that will be required to be submitted by the applicant will depend on the project, ownership structure and whether it is an ongoing or start-up business. In general, the information required is outlined in the BLP checklist in the exhibits.

The financial analysis will differ depending on whether the business is a start-up or existing business. The analysis will include for existing businesses a spread of the current and financial statements to determine trends. The pro forma statements will then be compared to these past statements. Financial ratios will be analyzed. The statements and ratios will be compared to industry averages. For start-up business the projections will be analyzed and ratios developed, and both compared to industry averages.

Ratios that will be analyzed include:

- Current Ratio: Current assets/current liabilities. This ratio is a rough indication of a firm's ability to service its current obligations. A ratio of 2:1 is considered secure.
- Quick Ratio: Cash & equivalents plus accountants & notes receivable/current liabilities. The ratio is a refinement of the current ratio. A ratio of 1:1 usually indicates ample liquidity.

- Cash Flow Coverage: Net profit & depreciation & depletion-amortization expenses/current portion of long term debt. This ratio is a measure of the ability to service long term debt.
- Another coverage ratio is: Earnings before interest and taxes/annual interest expenses. This ratio is a measure of a firm's ability to meet interest payments. A Cash Flow Coverage of 1.25 debt service shall be used as a guideline.
- Debt to Worth: Total liabilities/tangible net worth. This ratio is the relationship between debt and a businesses net worth. A lower ratio is an indication of greater long-term financial safety and greater flexibility to borrow. In general, a Debt to Worth ratio of higher than 5:1 should not be exceeded as an underwriting policy. There are exceptions when the industry average is high due to its capital intensive nature or when projections show the ratio lowering quickly.
- Collateral Coverage: The value of collateral as compared to the amount of the loan. Typical underwriting guidelines suggest that 125% of loan balance be used. However, this is highly dependent on the quality and security of the collateral. In addition, collateral requirements are a cause of "financial gaps". The BLP shall use 125% as a guideline, which shall only be lowered with specific and detailed analysis and explanation.
- Break-Even Analysis: The analysis of the project's ability to support the projected labor costs and additional debt service at its break-even point (BEP) will be analyzed to determine what proportion of the jobs can be supported at that BEP. This will serve as a worst case look at the business' prospects for success, ability to service new debt, etc.

The financial and ratio analyses must be supported by the business plan. The business plan must provide a clear understanding of the project, competition, market strategy, sales estimates, management capacity and other factors.

Lastly, to ensure project feasibility, an evaluation will be conducted of the experience and capacity of the business principals to manage the business and achieve the projections.

Procedures:

1. Perform financial underwriting analysis.
   a. Spread historical financial statement and projections. Identify any significant differences and compare to industry averages.
   b. Review assumptions to projections. Determine if projections are reasonable and supported by market studies, business plan, and historical trends.
   c. Review financial ratios for project and compare to industry averages. If significantly different, determine the reasons and impact on feasibility.
   d. Review cash flow for project. Determine if there is adequate working capital.
   e. Determine break-even point for project, and how much the projections are above the break-even point. Determine if the public benefit will be realized at the break-even point.
2. Review the business plan, market information, historical financial statements, projections, ratio analysis, break even analysis, spreadsheet analysis, and management capacity to determine the project feasibility.
3. Sources of information:
   a. Historical Financial Statement;
   b. Financial Projections;
   c. Business Plan;
   d. Market and Industry information; and
   e. Industry Averages.

8.1 (F) Return on Equity Investment

The return on equity investment is the amount of cash that the investor/business owner is projected to receive in relation to their initial equity. For a sole proprietor, this equates to salary plus net income. To the extent practicable, the BLP should not provide more than a reasonable return on investment to the business owner. This will help ensure that the BLP will maximize the use of BLP funds and not unduly enrich the business owner/investor. However, care shall be taken to ensure that the rate of return will not be too low, so that the business owner's motivation remains high to pursue the business with vigor.

If the project's financial returns are projected to be too low to motivate the business and/or investor to proceed with the project then risks of the project outweigh the returns. An inadequate rate of return, adjusted for industry and locational risks, is a third method to determine the gap appropriate to be funded with BLP funds. To analyze this gap, the projected return on investment must be compared to the return on investment on similar projects. If it is shown that a gap does exist, then the BLP financing rate and terms must be set at a rate that provides a return equal to the "market rate". Real estate appraisers and lenders are important sources of information on "market rate" returns.

Procedures:

1. Review projections.
    a. Review revenues, expenses (including officer's salary/owners' draw), debt service and net operating income, and compare to historical financial information and to industry averages. Determine if these items are reasonable.
    b. Review indicators of owners' return on equity, including officers' salary, owners' draw, and net operating income. Given the project's risk and local conditions, determine if the return on equity is reasonable compared to industry averages.
2. Review the business and personal obligations. Determine what return on equity is necessary to meet personal and business obligations.
3. If return on equity is above industry averages, adjusted for risk and local conditions, take steps to reduce the return to within a reasonable rate by restricting owners' draw/officers' salary, or adjusting the BLP loan terms.
4. If return is below average, adjust BLP subsidy to bring the rate of return closer to the industry average.
5. Sources of information:
    a. Financial projections;
    b. Historical financial statements;
    c. Personal financial statements; and
    d. Industry averages.

8.1 (G) Disbursement of BLP Funds on a Pro Rata Basis

To the extent practicable, BLP funds should be disbursed on a pro rata basis with other funding sources to avoid placing BLP funds at a greater risk than other funding sources. When it is determined that it is not practicable to disburse BLP funds on a pro rata basis, other steps shall be taken to safeguard BLP funds in the event of a default.

Procedures:

1. Review Sources and Uses of Funds. Determine when BLP funds will be expended as compared to other funds.
2. Determine other funding sources' policies towards expenditure of funds. These policies may require the use of BLP funds first. If so, may need to negotiate with other funding sources.

3. If BLP funds are to be expended first, consider actions to safeguard BLP funds (e.g. performance or completion bonds).
4. Sources of information:
    a. Sources and Uses of Funds
    b. Construction Contracts; and
    c. Lender Requirements/Policies.

8.1 (H) Standards for Evaluating Public Benefit

Each project will be reviewed to determine if a minimum level of public benefit will be obtained from the expenditure of BLP funds. The minimum standards are:

- The project must lead to the creation or retention of at least one full-time equivalent (FTE) job per $35,000 of BLP funds used; or
- The project must provide goods or services to residents of an area, such that the number of TIG persons residing the areas served by the project amounts to at least one TIG person per $350 of BLP funds used.

Procedures:

1. Review historical financial statements.
    a. Review historical labor costs as a percentage of revenues. Compare the percentage to projected labor costs. Determine if the two figures are consistent. If not, obtain an explanation.
    b. Determine if the number of projected jobs is consistent with the projected increase in labor costs. Compare the labor costs percentage to industry averages.
2. Review the projections.
    a. Determine if the assumptions used to project revenues and labor costs are reasonable. Determine if market/industry information and historical financial statements support revenues and labor costs.
3. Determine if project meets minimum public benefit requirements (one full-time equivalent job for every $35,000 in BLP funds, or one TIG resident per $350 in BLP funds residing in the area served by the project).
4. For infrastructure projects, determine the area of benefit; negotiate fair share contributions; develop, execute, and implement fair share agreement; and track jobs from the benefiting business(s) if the projected cost/job is less than $10,000, or track jobs in the area of benefit if the projected cost per job is $10,000 or more.

IX. BUSINESS LOAN PROGRAM (BLP) TASK MATRIX

TASK	COUNTY STAFF	COUNTY
Establish and Maintain Program Loan Files		X
Legal Review of Loan Documents		X
Approve BLP Guidelines		X
Prepare Fiscal/Performance Reports		X
Review Fiscal/Performance Reports		X
Monitor County Staff		X
Conduct Environmental Reviews		X
Participate in LAB Review		X
Lo an Servicing and Accounting		X
Provide Monthly Receipts of Loan Payments		X
Provide Quarterly Statements on Loans		X
Implement Collections and Foreclosures		X
Approve Reuse Plan		X

TASK	COUNTY STAFF	COUNTY
Meet with Participating Lenders		X
Publicize and Market the BLP		X
Screen and Assist Loan Applicants		X
Refer Ineligible Applicants to Others		X
Request Preliminary Loan Information		X
Get Credit Report, Other Documentation		X
Prepare Loan Package and Recommendation with Appropriate Determination		X
Present Loan to LAB		X
Close Loan with Other Lenders		X
Monitor Loan and General Compliance		X
Prepare and Sign all HCD Reports		X
Prepare Cash Requests and HCD Reports		X
Clear Special Conditions		X
Site Visits to Borrowers		X
Track Jobs/Benefit (EEO)		X
Monitor Labor Standards		X
Income Screening/TIG Benefit		X
Conduct Appeal Process		X
Planning, Building & Public Works Reviews		X
Attend HCD Workshops		X
Refer for Business Counseling - SBDC		X
Provide Overall Review and Liaison Between BLP Components, County Staff, County and CDBG Program		X

X. CDBG MONITORING

10.1 Environmental Review

Once a loan is determined to be viable under the CDBG criteria, staff will work to initiate the Environmental Review process for the project specific activity. Environmental review procedures are included.

CDBG monitoring requirements will vary depending on the use of funds and the applicable federal overlays.

10.2 Public Benefit Requirements

Job Creation/TIG Benefit
See **Section 8.1 (H)** for project evaluation criteria. The El Dorado County Department of Housing, Community and Economic Development will be responsible for the Income Certification processes.

10.3 Labor Standards Requirements

CDBG loans may trigger compliance with Federal Labor standards and provisions. The following CDBG-assisted projects may be subject to the payment of Federal prevailing wage rates:

- New construction or rehabilitation
- On-site improvements in support of new construction

- Installation of equipment

When a project is determined to be subject to Federal labor standards, the County will be responsible for assigning in-house or contract staff to monitor compliance with this requirement.

10.4 Other Monitoring Requirements

Other requirements that apply to CDBG funding and may need to be monitored for compliance include:

- **Acquisition, Anti-Displacement, and Relocation.** If the County uses CDBG funds to acquire property, then it must comply with CDBG acquisition procedures. The County must minimize the displacement of persons (families, individuals, businesses, non-profit organizations, and farms) that may result from CDBG-funded activities. (24 CFR 570.606). If the displacement occurs, then the grantee must insure that the affected parties are provided with adequate relation assistance (24 CFR 570.606).
- **Equal Opportunity/Section 3.** The County must insure that no one is being excluded from participating in, or benefiting form, the CDBG program on the basis of race, color, religion, national origin, or sex (24 CFR 570.602). The County must have a system in place for tracking the “protected class” status of loan applicants, loan recipients, job applicants, and job recipients (24 CFR 570.607).
- **Procurement.** The County will utilize procedures in procuring services, supplies, equipment and construction contracts that maximize free and open competition and the efficient, economical use of the CDBG funds (24 CFR 85.36).
- **Contractor Eligibility and Certification.** The County will ensure that contractors are not on the federal list of ineligible contractors and that they are licensed and in good standing (24 CFR 570.609).

El DORADO COUNTY
MICROENTERPRISE LOAN PROGRAM GUIDELINES

I. PURPOSE:

The El Dorado County Microenterprise Assistance Loan Program (MLP) is designed to provide the critical and necessary capital needs of businesses and development projects in El Dorado County. The MLP is capitalized with funds from the State of California Community Development Block Grant (CDBG) Program. The intent of the MLP is to provide appropriate assistance to business and development projects, which in turn will create and/or retain jobs, along with increasing the commercial and industrial base of the community.

The MLP provides loans in which repayments are "revolved" or "recycled" to be loaned again in the same program. Therefore, the initial funds that capitalize the program will be used again to create additional jobs, assist more businesses and projects and provide significant benefits beyond the MLP's initial loans.

The MLP is designed to provide need-based funding as some percentage of a project's total financing requirements. The MLP is targeted to businesses and projects that have the greatest potential for long-term job creation/retention, particularly jobs created and/or retained for low and moderate income persons.

The MLP will assist businesses and projects that start-up, expand, and/or locate within the unincorporated county limits of El Dorado. The MLP funds can be used to finance:

- Working Capital/Lines of Credit,
- Inventory Purchase,
- Equipment Acquisition,
- Furniture/Fixtures.

II. POLICY:

The following elements are critical in the selection of loans for the MLP Program:

- Existence of a documented need that hinders the business or project from obtaining or affording the project without the MLP injection.

- The loan meets the MLP's underwriting criteria.

- Business owner qualifies as a CDBG Microenterprise (i.e. owner(s) is Target Income Group, defined as household earnings at or below 80% of the area median income for El Dorado County adjusted for household size, and that the business has five or fewer employees, including the owner(s.))

- The terms and conditions of the project are appropriate.

III. SOURCE OF FUNDING:

The source of funding for the MLP is the State of California Community Development Block Grant Program Enterprise Fund Component Program. Loans are not made from the El Dorado County General Fund.

IV. DESCRIPTION OF FUNDING

4.1 Guidelines

Loans will range from a minimum of $1,000 to a maximum of $25,000. However, MLP loans above $25,000 will require additional approval by the State Department of Housing and Community Development (HCD), Economic Development Advisory Committee (EDAC).

- **Leveraging**: Minimum 10% of total project costs.

- **Loan Terms:** Up to ten years, depending on the asset being financed and the demonstrated need for the MLP funds. The length of the loan shall not exceed the economical life of the equipment/asset being financed.

- **Interest Rate:** The interest rate is set based on the demonstrated financial need of each borrower. If the financial need is the availability of capital, the interest rate shall be near market rates for the asset being financed. If the financial need is the cost of capital (rate, term or collateral requirements), then the interest rate is set by evaluating the financial information to determine at what interest rate the project would be viable.

- **Loan Fee:** Borrowers will pay for any direct costs incurred in loan processing and closing, such as recording fees, attorney fees, escrow fees, etc.

- **Prepayment Penalty:** None

- **Deferral of Payments:** On a case by case basis, determined based on the financial "gap."

- **Collateral Requirements**: All MLP loans shall be fully secured by collateral in order to maintain the Microenterprise Loan Program. No unsecured loans shall be made. Collateral will usually be in the form of liens on the assets financed including fixed assets such as machinery, accounts receivable, inventory, and lease assignments. Liens upon other non-project assets of the borrower may also be used to secure the loan. Personal guarantees will be required of all person/entities holding a 50% or more interest in the applicant's business. Types of collateral may include

    - Liens on real property,
    - Deeds of Trust,
    - Liens on machinery, equipment, or other fixtures,
    - Lease assignments, as appropriate,
    - Personal and/or corporate guarantees, as appropriate, and
    - Other collateral, as appropriate.

4.2 General Administrative Features

The Microenterprise Loan Program will comply with all CDBG requirements, including, but not limited to:

- Confidentiality of Client Financial Information, as allowed by law;
- Equal Opportunity/Affirmative Action Policy;
- Attorney review of all contracts and legal forms;
- Monitoring and Reporting Forms;
- Collection and Foreclosure Policy;
- Labor Standards (where applicable);
- Clearing CDBG Special Conditions;
- Relocation assistance (where applicable);
- Section 3 requirements;
- Fair Housing requirements;
- Environmental reviews;
- El Dorado County staff will be responsible for overall project marketing, loan evaluation, loan packaging, and monitoring.

4.3 Project Evaluation Criteria

The following evaluation criteria will be adhered to during the course of the Microenterprise Loan Program:

- The number of jobs created/retained and the percentage benefiting members of the Targeted Income Group.
- The amount of private dollars leveraging MLP funds.
- The financial viability of the proposed project.
- The demonstrated need for the MLP funds.

4.4 General Credit Requirements

A loan applicant must:

- Show ability to operate a business successfully,
- Have enough borrowing ability or equity to operate, with the MLP loan, on a sound financial basis,
- Show the proposed loan is of sound value or reasonably secure to assure repayment, and
- Show that the past earning record and future prospects of the firm indicate ability to repay the loan and other fixed debt, if any, out of the profits.

4.5 Loan Packaging

County staff will be responsible for MLP loan packaging activities, including review of all proposals presented to the Loan Advisory Board (LAB).

4.6 Loan Review

The Loan Advisory Board (LAB) shall be responsible for reviewing funding proposals and making recommendations to County staff. The El Dorado County Housing and Community Development Agency will decide terms and conditions of loan agreements. The LAB shall be comprised of:

- One representative of County Staff;
- One Certified Public Accountant;
- Two representatives of a El Dorado County lending institution, and
- Two representative of the business community appointed by the County.

HCD/CDBG will make the final loan determination after County LAB approval.

4.7 Length of Review Process

On average, the MLP review process takes six to eight weeks from submittal of a complete loan application through LAB review. Loan funds can be disbursed two to three weeks after signing the MLP documents, depending on the financing and approval by HCD. Conditional commitments can be made prior to final approval from another funding source. Every effort will be made to facilitate the process to coincide with the other funding source and the project's requirements.

4.8 Linking Jobs with Long-Term Unemployed

County staff will work closely with the Workforce Investment Act (WIA) programs and services that provide assistance to the unemployed and low and moderate income persons. Early and consistent involvement with each loan applicant will be an integral policy of the MLP Program.

V. ELIGIBILITY

5.1 Eligible Applicants

In order to be considered for financing through the MLP, applicants must meet the following requirements:

- Have a completed business plan which includes a competitive market analysis and qualify as a Microenterprise (owner(s) is TIG and the business has five or fewer employees, including the owner(s))
- Be an on-going or start-up private, for profit Microenterprise business concern, partnership, sole proprietorship licensed and located (or planning to locate) within the unincorporated areas of El Dorado County. Businesses operating out of a residence are eligible.
- Be in compliance with all county, state and federal financial obligations, including taxes with zoning regulations.
- Loan monies may NOT be used to satisfy any existing debts.

Conflict of Interest

When the County's program contains Federal funds, the following shall be addressed: in accordance with title 24, Section 570.611 of the Code of Federal Regulations, no member of the governing body and no official, employee or agent of the local government, nor any other person who exercises policy or decision-making responsibilities (including members of the loan committee and officers, employees, and agents of the loan committee, the administrative agent, contractors and similar agencies) in connection with the planning and implementation of the Program shall directly or indirectly be eligible for this Program. This ineligibility shall continue for one year after an individual's relationship with the County ends. Exceptions to this policy can be made only after public disclosure and formal approval by the governing body of the locality.

5.2 Eligible Uses

The project must be commercial or industrial. MLP funds can be used for construction and permanent financing, working capital, inventory, equipment, real property acquisition, construction and rehabilitation.

5.3 Ineligible Uses

Projects must be located in the unincorporated areas of El Dorado County. Projects cannot be residential in nature. Projects must have reasonable assurance of repayment. Projects are not eligible if they create a conflict of interest pursuant to California Government Code S87100 et seq for any current El Dorado County or Business Development Corporation employee or Loan Advisory Board (LAB) member. Projects must create or retain jobs, primarily for the Targeted Income Group and must leverage private or equity funds.

5.4 Eligible Costs

- Finance of inventory, furniture, fixtures, machinery and equipment.
- Working capital, supplies and start up costs.

5.5 Ineligible Costs for CDBG Loans

Costs incurred prior to CDBG grant execution, submittal of the loan application, and environmental review requirements, except for private leverage as specified in Section 4.1. and costs other than those listed as eligible in Section 5.5.

VI. ROLE OF THE COUNTY

6.1 County staff will, as required

- Publicize and market the MLP; screen all applicants for loans;
- Refer candidates that are not eligible, do not meet the MLP criteria or need technical assistance to the Small Business Development Center;
- Ask promising candidates to submit preliminary information and an application, along with accompanying financial information;
- Prepare package, along with recommendation to loan advisory;
- If approved, assist with loan processing and closing;
- Once closed, monitor the loan, maintain the loan records, and monitor compliance with job objectives.

The County staff will make the daily decisions called for or implied regarding the activities of the MLP. Decisions to foreclose and declare defaults will be the responsibility of the El Dorado County Housing and Community Development Agency, in consultation with legal counsel, based upon recommendations of staff. County staff will monitor on-going operations of the loan recipient. Staff will consult and monitor program operator during the term of the contract. Staff will review all reports, financial information and performance reports on each loan during the term of the loan. Staff will serve as the contact for the State Department of Housing & Community Development for the MLP.

County staff will meet with each MLP applicant to ensure that the applicant maintains the documentation required. Staff will brief each applicant on his obligations and requirements of the Program. Additionally, County staff will conduct an environmental review of the project as necessary. County staff and program operator will refer potential applicants, including those ineligible or denied MLP financing, that need technical and management assistance to the appropriate organization. As a condition of the loan, the County or LAB may require that applicants receive pre- and/or post-loan counseling.

County staff and/or the program operator may require applicants who have received loans to undertake business counseling if it appears that the applicant's financial position is declining and the MLP loan may become delinquent.

6.2 Role of the Loan Collection Agent

The County will conduct the duties of the loan collection agent. The duties will include the following:

- Loan servicing and accounting;
- Provide monthly receipts of loan payments
- Provide quarterly statements on each loan
- In concurrence with the jurisdiction's legal counsel, undertake loan collections, including asset liquidation;
- Obtain credit reports on all loan applicants

VII. LOAN SELECTION & APPROVAL PROCESS

7.1 (A) Marketing

The marketing of the MLP Program will be accomplished by a variety of means. There will be media coverage, marketing brochures, and joint marketing through program operator's existing loan packaging and financial services. Local lenders will recommend clients and projects, when appropriate. The Small Business Development Center, local Realtors, and business associations will also refer potential applicants. The County will also use existing business and community networks to market the MLP Program.

7.1 (B) Procedure

Once a potential project has been identified, County staff will conduct a preliminary review for eligibility with the MLP criteria. If another lending source is more appropriate, or the project does not meet the MLP criteria, the staff will refer the prospective borrower to another organization for assistance.

If the project appears to meet the criteria, the applicant will be asked to submit preliminary information. Preparation and submission by an applicant of preliminary information and supporting documents include, but are not limited to: business and personal tax returns for the last three years or since commencement of operations (whichever is less), business financial statements (balance sheet and income statement) for current year and prior three years, current personal financial statement, credit history, and proposed project summary. Start-up businesses must submit proforma financial statements for the first five years. Real estate projects must submit pro forma projections for the first five years, and pre-leasing information.

The preliminary information will be reviewed by County staff. If the project is viable, a draft loan analysis will be prepared by program operator. If the decision is to decline the request, the program operator will provide the applicant with a written explanation of the denial. If appropriate, referrals to other organizations will be made.

If the review is positive, the applicant will be invited to an application conference with program operator and to submit a formal application to program operator, which will be presented to the LAB for their recommendation. At the application conference, program operator will review with the applicant the formal MLP checklist and required information, forms and financial schedules deemed necessary the County to complete the loan package. The County will determine project needs/conformance with local requirements, as well as determine the necessary environmental review for the project. The County will begin the environmental review as necessary.

The applicant, in conjunction with the County will develop the employment plan. Upon completion of the necessary information, applications will be presented by the program operator to the LAB. The presentation will include a completed MLP Project Evaluation Form. If the private funds are from equity, then the commitment letter must be from the applicant. The program operator presentation will include a recommendation. This recommendation will include the proposed terms and conditions, based upon the identified financial need and the "appropriate" analysis undertaken by program operator, along with a checklist insuring that the loan meets the MLP guidelines and criteria.

The LAB will decide to recommend approval or to decline the loan request. If declined the applicant will be informed in writing by the County as to the reason. If recommended, the LAB's recommendation can be under the terms and conditions proposed by program operator, or the LAB can recommend alternative terms and conditions. The LAB recommendation is the presented to the County Staff. County staff will review the loan package for completeness and regulatory compliance, as well as final review for compliance with MLP guidelines and criteria.

When the County approves or denies the loan request, the applicant will be notified in writing. If denied, the reasons for denial will be included. County approval shall include a certification statement that, based on his/her review of the staff report and LAB recommendation, the County finds that the CDBG loan is appropriate and that the assistance is commensurate with both the needs of the borrower and public benefits stemming from the project.

7.1(C) Loan Closing

Upon approval by the County will prepare for the loan closing. After final approval from HCD/CDBG the Borrower will sign all the necessary documents and agreements. The County will request a drawdown of funds from the State Department of Housing & Community Development (the timing of the request may vary depending on the project). The County will prepare the loan closing documents, prepare title and lien searches, and UCC-1 filings, if appropriate. County legal counsel will review all agreements and documents, as necessary.

Loan closing will be undertaken by the County. At the time of closing, the Borrower will be provided with a checklist outlining their obligations under the MLP Program. At closing, or another specified time, funds will be disbursed to the Borrower. The County will complete any remaining legal, regulatory or other items. Monitoring and compliance files will be set-up at this time.

7.1(D) Loan Monitoring

Two separate loan files will be maintained. The first is the legal file which holds all the original loan documentation, along with the original documents. This file shall be kept in a fireproof vault for safekeeping. The second is a credit file which shall contain the day-to day administrative records of the loan. At a minimum the legal file shall include:

- Note
- Loan Agreement, including Non-Financial Employment Plan
- Mortgage
- General Security Agreement
- Personal Guaranty
- Corporate Guaranty
- Subordination Agreement
- Life Insurance Policy and Assignment
- Hazard Insurance Policy and Assignment
- General Resolution
- Certificate of Secretary
- Opinion of Counsel
- Intercreditor Agreement

The credit file shall contain, at a minimum, the loan application and financial information associated with the application, credit memo, LAB recommendation, final local approval, disbursement records, reports of site visits, updated financial information provided by borrower, job creation/retention data, etc.

A reporting system will be established for each loan and the loan portfolio as a whole. The report should be up-dated at least quarterly. The County shall be responsible for preparation of this report. The report will be used by the County to monitor the loans and identify problems. The report will contain the following:

- **Fund Report Balance:** A monthly summary of the beginning fund balance, principal and interest recaptured during the month, disbursements made during the month and funds committed but not yet disbursed, and amount remaining in the MLP which is unencumbered. The monthly receipts from the lender on each loan will serve as the basis for this report.

- **Portfolio Summary Report:** A quarterly summary of the total loans outstanding and authorized loans. The report shall include a quarterly statement on each loan, prepared by the lender. The quarterly report shall include the last payment date and loan balance. Delinquent loans shall be identified and a summary of actions to date to collect delinquent loans shall be included.

- **Employment Report:** A quarterly report on each project detailing the jobs created/retained, and where applicable those hired that meet the Targeted Income Group.

- **Loan Loss and Delinquent File:** A list of all loans that have been classified as uncollectible and a summary of foreclosure procedures to date on the loan. Loans that are delinquent will also be listed, along with a summary of recommended steps, and steps taken to date.

- **Tickler File:** A listing of the current loan portfolio and dates for receipt of financial statements, employment information, renewal of UCC-1 filings, review date, dates for insurance renewal and other information.

In addition, a loan monitoring file will be established which will include a summary of the monitoring requirements of the State Department of Housing and Community Development. A tickler file will be part of this overall file to insure that loan and MLP monitoring is undertaken and completed

VIII. LOAN UNDERWRITING

The loan underwriting policies of the El Dorado County Microenterprise Loan Program (MLP) are designed to insure the program's ongoing viability, assist businesses that could not proceed without the MLP, and ensure that the MLP assistance is appropriate.

8.1 HUD Underwriting Guidelines

The County has adopted the HUD underwriting guidelines for the MLP to determine whether a proposed CDBG subsidy is appropriate to assist with business expansion or retention. In addition, the project will be reviewed to determine that a minimum level of **public benefit** will be obtained form the expenditure of the CDBG funds in support of the project.

The objectives of the underwriting guidelines are to ensure that:

- Project costs are reasonable;
- All sources of project financing are committed;
- To the extent practicable, MLP funds are not substituted for non-Federal financial support;
- The project is financially feasible;
- To the extent practicable, the return on the owner's equity investment will not be unreasonably high;
- To the extent practicable, MLP funds are disbursed on a pro rata basis with other financing provided to the project; and
- Sufficient public benefit will be received from the expenditure of MLP funds.

8.1(A) Project Costs are Reasonable

All project costs will be reviewed for reasonableness, and to avoid providing either too much or too little MLP assistance. The amount of time and resources expended evaluating the reasonableness of a cost element shall be commensurate with its costs. In some instances, it will be necessary to obtain third-party, fair-market price quotations or a cost element. Particular attention will be documenting the cost elements in non-arms-length transactions.

Procedures:

1. Start with Sources and Uses of Funds.
2. For each Use of funds, determine if costs are reasonable.
    a. For machinery, equipment. Determine if the costs are estimated by a third-party (e.g. architect, engineer, equipment supplier, etc.). Determine if the estimates are included in the application. Determine if the contingency is adequate.
    b. For working capital, compare the amount of working capital to industry averages, risk, historical needs of the business and the projected need. Analyze business financial statements, projections, operating cycle and financial ratios.
3. A higher level of review will be required if there are no third party estimates.
4. Sources of information:
    - Sources and Uses of Funds Statement;
    - Financial Statements and Projections;
    - Industry Averages (Robert Morris):

- Third Party Costs Estimates;
- Building Department/Public Works;
- Realtors;
- Appraisers;
- Architects/Engineers;
- Contractors;
- Equipment Suppliers; and
- Other similar projects.

8.1 (B) Commitment of All Sources of Project Financing

Prior to the commitment of MLP funds to the project, a review shall be conducted to determine if sufficient sources of funds have been identified and committed to the project, and the participating parties have the financial capacity to provide the funds to ascertain if the project is viable and will move ahead in a timely manner. In certain circumstances, the MLP may commit its funds in advance of final commitments from other funding sources. However, to conduct the underwriting analysis, the approximate terms and conditions of the other funding sources should be known. Final commitments from the other funding sources will be required, with substantially similar terms and conditions as used in the underwriting analysis, prior to any loan closing or disbursement of funds.

Procedures:

1. Start with Sources and Uses Form.
    a. For all sources of funds, determine if there is evidence verifying commitment or intent to commit.
    b. For debt sources, be in receipt of letters of intent or interest, which specify the level of commitment and terms/conditions of the loan. The proposed terms should be reflected in the business projected debt schedule and in the financial projections. Determine if actual loan packages have been submitted to lenders.
    c. For equity sources, determine if the equity injection is verified on the business or personal financial statements. Or if an investor provides the equity, obtain evidence of the level and terms of commitment (e.g. letter of intent with accompanying financial statement verifying availability of funds).
2. Sources of information:
    a. Sources and Uses of Funds,
    b. Business and Personal Financial Statements, and
    c. Letters of intent/interest form lenders, partners and investors.

8.1 (C) Avoid Substitution of CDBG Funds for Non-Federal Financial Support

The project will be reviewed to ensure that, to the extent practicable, MLP funds will not be used to substantially reduce the amount of non-federal financial support for the project to make the most efficient use of the MLP funds.

8.1 (D) Financial Feasibility of the Project

Each project will be examined to determine the financial viability of the project, and thus the reasonable assurance that the public benefit will be realized. The current and past financial statements for both the business and individuals must be analyzed, along with tax returns and projections. The assumptions behind the projections must be critically analyzed. Income and expense costs shall be evaluated and compared historically, where applicable, and compared to industry averages (using guides such as Robert Morris' Annual Financial Statements). Project costs, including both hard and soft costs, must be determined to be reasonable. Accurate project costs are vital to determining project feasibility.

As part of the financial analysis, the past, current, and projected financial data shall be analyzed to determine if the job estimates are reasonable and supportable. Labor costs shall be looked at the break-even point. In addition, labor costs shall be checked against industry averages. Variations should be explained in the loan analysis.

The terms and conditions of the MLP loan must be appropriate. In general, the interest rate shall be set at a rate where available cash flow is able to meet debt obligations, after other obligations are met, with enough cash flow remaining to operate successfully. The loan term typically is based in the asset being financed. The term should not exceed the economic life of the asset being financed. However, a longer loan amortization schedule, with the loan due at the end of the economic life may be justifiable

Each loan shall include a written explanation of the appropriate analysis that was undertaken, and the reason the terms and conditions of the loan were approved.

8.1 (E) Financial Analysis

Historical and projected financial statements will be subject to financial analysis to determine the gap, and structure the terms and conditions of the MLP loan, as discussed above, but also to determine that the project is feasible. In addition, use prudent underwriting guidelines, demonstrating that the proposed loan is of sound value, and note how past earnings and future prospects indicate an ability to meet debt obligations out of profit.

Information that will be required to be submitted by the applicant will depend on the project, ownership structure and whether it is an ongoing or start-up business. In general, the information required is outlined in the MLP checklist in the exhibits.

The financial analysis will differ depending on whether the business is a start-up or existing business. The analysis will include for existing businesses a spread of the current and financial statements to determine trends. The pro forma statements will then be compared to these past statements. Financial ratios will be analyzed. The statements and ratios will be compared to industry averages. For start-up business the projections will be analyzed and ratios developed, and both compared to industry averages.

Ratios that will be analyzed include:

- Current Ratio: Current assets/current liabilities. This ratio is a rough indication of a firm’s ability to service its current obligations. A ratio of 2:1 is considered secure.
- Quick Ratio: Cash & equivalents plus accountants & notes receivable/current liabilities. The ratio is a refinement of the current ratio. A ratio of 1:1 usually indicates ample liquidity.
- Cash Flow Coverage: Net profit & depreciation & depletion-amortization expenses/current portion of long term debt. This ratio is a measure of the ability to service long term debt.
- Another coverage ratio is: Earnings before interest and taxes/annual interest expenses. This ratio is a measure of a firm’s ability to meet interest payments. A Cash Flow Coverage of 1.25 debt service shall be used as a guideline.
- Debt to Worth: Total liabilities/tangible net worth. This ratio is the relationship between debt and a businesses net worth. A lower ratio is an indication of greater long-term financial safety and greater flexibility to borrow. In general, a Debt to Worth ratio of higher than 5:1 should not be exceeded as an underwriting policy. There are exceptions when the industry average is high due to its capital intensive nature or when projections show the ratio lowering quickly.
- Collateral Coverage: The value of collateral as compared to the amount of the loan. Typical underwriting guidelines suggest that 125% of loan balance be used. However, this is highly dependent on the quality and security of the

collateral. In addition, collateral requirements are a cause of “financial gaps”. The MLP shall use 125% as a guideline, which shall only be lowered with specific and detailed analysis and explanation.

- Break-Even Analysis: The analysis of the project’s ability to support the projected labor costs and additional debt service at its break-even point (BEP) will be analyzed to determine what proportion of the jobs can be supported at that BEP. This will serve as a worst case look at the business’ prospects for success, ability to service new debt, etc.

The financial and ratio analyses must be supported by the business plan. The business plan must provide a clear understanding of the project, competition, market strategy, sales estimates, management capacity and other factors.

Lastly, to ensure project feasibility, an evaluation will be conducted of the experience and capacity of the business principals to manage the business and achieve the projections.

Procedures:

1. Perform financial underwriting analysis.
    a. Spread historical financial statement sand projections. Identify any significant differences and compare to industry averages.
    b. Review assumptions to projections. Determine if projections are reasonable and supported by market studies, business plan, and historical trends.
    c. Review financial ratios for project and compare to industry averages. If significantly different, determine the reasons and impact on feasibility.
    d. Review cash flow for project. Determine if there is adequate working capital.
    e. Determine break-even point for project, and how much the projections are above the break-even point. Determine if the public benefit will be realized at the break-even point.
2. Review the business plan, market information, historical financial statements, projections, ratio analysis, break even analysis, spreadsheet analysis, and management capacity to determine the project feasibility.
3. Sources of information:
    a. Historical Financial Statement;
    b. Financial Projections;
    c. Business Plan;
    d. Market and Industry information; and
    e. Industry Averages.

8.1 (F) Return on Equity Investment

The return on equity investment is the amount of cash that the investor/business owner is projected to receive in relation to their initial equity. For a sole proprietor, this equates to salary plus net income. To the extent practicable, the MLP should not provide more than a reasonable return on investment to the business owner. This will help ensure that the MLP will maximize the use of MLP funds and not unduly enrich the business owner. However, care shall be taken to ensure that the rate of return will not be too low, so that the business owner’s motivation remains high to pursue the business with vigor.

If the project’s financial returns are projected to be too low to motivate the business and/or investor to proceed with the project then risks of the project outweigh the returns. An inadequate rate of return, adjusted for industry and location risks, is a third method to determine the gap appropriate to be funded with MLP funds. To analyze this gap, the projected return on investment must be compared to the return on investment on similar projects. If it is shown that a gap does exist, then the MLP financing rate and terms must be set at a rate that provides a return equal to the “market rate”. Real estate appraisers and lenders are important sources of information on “market rate” returns.

Procedures:

1. Review projections.
    a. Review revenues, expenses (including officer's salary/owners' draw), debt service and net operating income, and compare to historical financial information and to industry averages. Determine if these items are reasonable.
    b. Review indicators of owners' return on equity, including officers' salary, owners' draw, and net operating income. Given the project's risk and local conditions, determine if the return on equity is reasonable compared to industry averages.
2. Review the business and personal obligations. Determine what return on equity is necessary to meet personal and business obligations.
3. If return on equity is above industry averages, adjusted for risk and local conditions, take steps to reduce the return to within a reasonable rate by restricting owners' draw/officers' salary, or adjusting the MLP loan terms.
4. If return is below average, adjust MLP subsidy to bring the rate of return closer to the industry average.
5. Sources of information:
    a. Financial projections;
    b. Historical financial statements;
    c. Personal financial statements; and
    d. Industry averages.

8.1 (G) Disbursement of MLP Funds on a Pro Rata Basis:

To the extent practicable, MLP funds should be disbursed on a pro rata basis with other funding sources to avoid placing MLP funds at a greater risk than other funding sources. When it is determined that it is not practicable to disburse MLP funds on a pro rata basis, other steps shall be taken to safeguard MLP funds in the event of a default.

Procedures:

1. Review Sources and Uses of Funds. Determine when MLP funds will be expended as compared to other funds.
2. Determine other funding sources' policies towards expenditure of funds. These policies may require the use of MLP funds first. If so, may need to negotiate with other funding sources.
3. If MLP funds are to be expended first, consider actions to safeguard MLP funds (e.g. performance or completion bonds).
4. Sources of information:
    a. Sources and Uses of Funds
    b. Construction Contracts; and
    c. Lender Requirements/Policies.

8.1 (H) Standards for Evaluating Public Benefit:

Each project will be reviewed to determine if a minimum level of public benefit will be obtained from the expenditure of MLP funds. The minimum standards are:

- The business owner must be a member of a low-moderate target income group.

Procedures:

1. Review historical financial statements.
    a. Review historical labor costs as a percentage of revenues. Compare the percentage to projected labor costs. Determine if the two figures are consistent. If not, obtain an explanation.
    b. Determine if the number of projected jobs is consistent with the projected increase in labor costs. Compare the labor costs percentage to industry averages.
2. Review the projections.

a. Determine if the assumptions used to project revenues and labor costs are reasonable. Determine if market/industry information and historical financial statements support revenues and labor costs.

3. Determine if project meets minimum public benefit requirements (business owner is TIG individual).

IX. MICROENTERPRISE LOAN PROGRAM (MLP) TASK MATRIX

TASK	COUNTY STAFF	COUNTY
Establish and Maintain Program Loan Files		X
Legal Review of Loan Documents		X
Approve MLP Guidelines		X
Prepare Fiscal/Performance Reports		X
Review Fiscal/Performance Reports		X
Monitor County Staff		X
Conduct Environmental Reviews		X
Participate in LAB Review		X
Loan Servicing and Accounting		X
Provide Monthly Receipts of Loan Payments		X
Provide Quarterly Statements on Loans		X
Implement Collections and Foreclosures		X
Approve Reuse Plan		X
Meet with Participating Lenders		X
Publicize and Market the MLP		X
Screen and Assist Loan Applicants		X
Refer Ineligible Applicants to Others		X
Request Preliminary Loan Information		X
Get Credit Report, Other Documentation		X
Prepare Loan Package and Recommendation with Appropriate Determination		X
Present Loan to LAB		X
Close Loan with Other Lenders		X
Monitor Loan and General Compliance		X
Prepare and Sign all HCD Reports		X
Prepare Cash Requests and HCD Reports		X
Clear Special Conditions		X
Site Visits to Borrowers		X
Track Jobs/Benefit (EEO)		X
Monitor Labor Standards		X
Income Screening/TIG Benefit		X
Conduct Appeal Process		X
Planning, Building & Public Works Reviews		X
Attend HCD Workshops		X
Refer for Business Counseling - SBDC		X
Provide Overall Review and Liaison Between MLP Components, County Staff, County and CDBG Program		X

X. CDBG MONITORING

10.1 Environmental Review

Once a loan is determined to be viable under the CDBG criteria, staff will work to initiate the Environmental Review process for the project specific activity. Environmental review procedures are included.

CDBG monitoring requirements will vary depending on the use of funds and the applicable federal overlays.

10.2 Public Benefit Requirements

Job Creation/TIG Benefit
See **Section 8.1 (H)** for project evaluation criteria. The El Dorado County Department of Housing, Community and Economic Development will be responsible for the Income Certification processes.

10.3 Labor Standards Requirements

CDBG loans may trigger compliance with Federal Labor standards and provisions. The following CDBG-assisted projects may be subject to the payment of Federal prevailing wage rates:

- New construction or rehabilitation
- On-site improvements in support of new construction
- Installation of equipment

When a project is determined to be subject to Federal labor standards, the County will be responsible for assigning in-house or contract staff to monitor compliance with this requirement.

10.4 Other Monitoring Requirements

Other requirements that apply to CDBG funding and may need to be monitored for compliance include:

- **Acquisition, Anti-Displacement, and Relocation.** If the County uses CDBG funds to acquire property, then it must comply with CDBG acquisition procedures. The County must minimize the displacement of persons (families, individuals, businesses, non-profit organizations, and farms) that may result from CDBG-funded activities. (24 CFR 570.606). If the displacement occurs, then the grantee must insure that the affected parties are provided with adequate relation assistance (24 CFR 570.606).
- **Equal Opportunity/Section 3.** The County must insure that no one is being excluded from participating in, or benefiting form, the CDBG program on the basis of race, color, religion, national origin, or sex (24 CFR 570.602). The County must have a system in place for tracking the “protected class” status of loan applicants, loan recipients, job applicants, and job recipients (24 CFR 570.607).
- **Procurement.** The County will utilize procedures in procuring services, supplies, equipment and construction contracts that maximize free and open competition and the efficient, economical use of the CDBG funds (24 CFR 85.36).
- **Contractor Eligibility and Certification.** The County will ensure that contractors are not on the federal list of ineligible contractors and that they are licensed and in good standing (24 CFR 570.609).