Montana State Small Business Credit Initiative 2.0
Loan Participation Program (MT SSBCI 2.0 LPP) Policy
Updated January 25, 2024

1. Program Overview

The American Rescue Plan Act of 2021 (ARPA) reauthorized and amended the Small Business Jobs Act of 2010 (SBJA) to provide $10 billion to fund the State Small Business Credit Initiative (SSBCI) as a response to the economic effects of the COVID-19 pandemic. SSBCI is a federal program administered by the Department of the Treasury (Treasury) that was created to strengthen state programs that support private financing to small businesses. SSBCI is expected to, in conjunction with new small business financing, create billions of dollars in lending and investments to **small businesses that are not getting the support they need to expand and create jobs**.

The MT SSBCI 2.0 Loan Participation Program (MT SSBCI 2.0 LPP) will be used to assist existing Montana businesses that need additional borrowings to stabilize, pivot, expand, or re-start their business and to assist new Montana businesses' entering the market. The MT SSBCI 2.0 LPP will partner with "<u>CDFI/RLFs</u>" throughout the state to identify small business in their regions that could benefit from the program.

Note: Underlined words in quotation marks, such as "<u>CDFI/RLFs</u>" above, are defined in the appropriate Section or in Section 20, starting on page 8 of this document.

2. Program Objectives

- Expand access to capital for underserved communities
- Assist in financing small businesses that are unable to access credit on reasonable terms
- Provide greater opportunity to rural and Native American entrepreneurs to create new businesses
- Partner with existing small businesses in attaining their growth goals
- Expand jobs and economic opportunities in Montana's rural counties and Indian country

3. 10:1 Leverage Requirement

The MT SSBCI 2.0 LPP must demonstrate a reasonable expectation that its program has the ability to use federal contributions to generate small business lending and investing of at least 10 times the federal contribution amount. *(Treasury Guidelines page 26)*

4. 1:1 Financing Requirement

The MT SSBCI 2.0 LPP must, at a minimum, require that $1 of public investment by the program will cause and result in $1 of new private financing. *(Treasury Guidelines page 28)*

"<u>Private financing</u>" means private financing across all approved state programs and includes all loans from a private source to an eligible borrower, whether occurring at or subsequent to loan closing (subject to certain Allocation Agreement restrictions regarding permissible types of subsequent private financing), and whether funded or unfunded. It encompasses term loans, lines of credit, and any new infusions of cash by the small business owner into the borrower. Private financing does <u>not</u> include financing provided by tax-credit supported vehicles, such as funds capitalized by the sale of state tax credits. *(Treasury Guidelines page 27)*

With this private investment financing requirement, a CDFI/RLF can act as both the primary and the participating lender in an MT SSBCI LPP loan, <u>only if</u> documentation is provided to the MT SSBCI 2.0 LPP certifying <u>the primary lender portion</u> of the funds <u>is not funded by or commingled with any federal, state, or local public funds</u>.

5. Assistance to VSBs and SEDI-Owned Businesses Requirement

The MT SSBCI 2.0 LPP must expend a portion of its allocation on loans to assist "<u>Very Small Businesses</u>" (VSBs) and "<u>Socially and economically-disadvantaged individual (SEDI) owned businesses</u>". *(Treasury Guidelines pages 8-13)*

6. Private Capital at Risk (PCAR)

Under MT SSBCI 2.0 LPP, lenders must risk a meaningful amount of their own capital resources given the preferred loan participation rate of 30/70 (30% MT SSBCI 2.0 LPP funds / 70% PCAR). The maximum participation rate is 50/50 (50% MT SSBCI 2.0 LPP funds / 50% PCAR). Lenders that transact with small businesses and bear the risk of loss in transactions (e.g., by originating loans supported by loan participation) have a meaningful amount of capital resources at risk if they bear 50 percent or more of the risk of loss in any transaction. A borrower's own funds, including borrower contributions to the transaction (sometimes referred to as borrower equity), do not qualify towards the 50 percent threshold. If such lenders transfer loans to debt investors, then the lenders must retain at least 5 percent of the risk of loss of the transaction. If a lender wishes to sell a portion of their retained participation amount of the MT SSBCI 2.0 LPP loan, they <u>must</u> receive written approval from the MT SSBCI 2.0 LPP prior to the sale. In addition, the lender <u>must</u> retain at least 5 percent of the risk of loss of the transaction. *(Treasury Guidelines page 29)*

7. Borrower/Loan Size Requirements

- Eligible borrowers must have fewer than 750 employees
- The MT SSBCI 2.0 LPP is targeting employers with fewer than 500 employees
- The MT SSBCI 2.0 LPP maximum participation amount is $1 million per eligible borrower *(Revised 01.20.2024)*
- The MT SSBCI 2.0 LPP will not provide credit if a given transaction exceeds $20,000,000 ($20 million)

(Treasury Guidelines pages 30-31)

8. A. Interest Rates

Interest rates will be fixed for the term of the loan as follows except as provided in Section 9 below:

- Up to 3-year term with monthly payments – 50 basis points (0.50%)
- 3-year up to 5-year term with monthly payments – 100 basis points (1.00%)
- 5-year up to 7-year term with monthly payments – 150 basis points (1.50%)

- 7-year up to 10-year term with monthly payments – 200 basis points (2.00%)
- Any intermediate term amortization will be at the next tier higher interest rate
- If amortization other than monthly, the MT SSBCI 2.0 Interest Rate will be increased by 50 basis points (0.50%)
- Lender service fee cannot exceed 50 basis points (0.50%)
- The servicing CDFI/RLF will be assessed an annualized 25 basis points (0.25%) service fee by MT SSBCI 2.0 LPP. The fee will be assessed on the calendar quarter on the balances of all outstanding loans.

B. Amortization *(added 10/31/2022)*

- The amortization period of a loan in which SSBCI participates must not exceed 20 years (240 months).
- The interest rate on the SSBCI participated portion of the loan is based on the amortization period of the loan, not to exceed 20 years.
- If a loan in which SSBCI participates has a maturity date other than the amortization period maturity date, SSBCI will expect to be paid off at the first maturity date, **UNLESS** the first maturity date is used to change the interest rate (variable interest rate), create a new maturity date, and payment. The lender must **ONLY** make a "Change in Terms" document and **NOT** change any other loan documents submitted to SSBCI as required in the SSBCI commitment letter.
- The SSBCI and lender participation percentage, as stated in the commitment letter, must remain the same for the duration of the loan.

9. Loan Term Requirements *(added 1/20/2024)*

- Maximum loan term of ten (10) years for real estate secured loans;
    i. Loan may be amortized over twenty (20) years.
        1. 10-year up to 15-year amortization with monthly payments – 250 basis points (2.50%)
        2. 15-year to 20-year amortization with monthly payments – 300 basis points (3.00%)
- Maximum loan term of seven (7) years for all other loans.
- MT SSBCI 2.0 LPP ultimately determines the participation balance of the loan and reserves the right to recommend a reduced amount or term.

10. Collateral Requirements

- The collateral must have sufficient value to support the debt and can be shared proportionately with the lender by the CDFI/RLF
- The collateral must have sufficient value to support the debt and can be in a subordinated position with the lender and/or CDFI/RLF
- Loan-to-Value is based on the lesser of the reasonable project costs (including architecture, engineering, and capitalized interest) or market value appraisal, whichever is less. The loan(s) must not be greater than the value of the collateral.
- Lender may require an attorney opinion on authority of borrower to borrow and all collateral documents

- MT SSBCI 2.0 participated loan documents must have a "Due on Sale" clause
- MT SSBCI 2.0 participated loan documents must not have a "Future Advance" clause
- MT SSBCI 2.0 participated loan documents must not have a "Cross Collateral" clause associated with other lender loans
- Any loan with an outstanding MT SSBCI 2.0 funded participation that is refinanced must have the participation portion of the loan paid off in full
- Other collateral as may be required by the lender, CDFI/RLF, and/or the MT SSBCI 2.0 LPP

11. Guarantees

- Personal or Corporate guarantees as required by the lender and/or CDFI/RLF
- For a Qualified Passive Company (Holding Company):
    - Operating company must be a guarantor or a co-borrower *(Treasury)*
    - Each natural person with a 20% or more ownership interest in the operating company or passive company must guarantee the loan *(Treasury)*

  (Treasury Guidelines pages 18-19)

12. Appraisal/Valuation

- Appraisal/Valuation as required by lender
- Licensed Montana appraisers are preferred unless specialized property collateral requires an out of state appraiser

13. Lending Protection Safeguards

In addition to any other federal or state law requirements, the MT SSBCI 2.0 LPP and their participants must conform to the below minimum national customer protection standards:

- Rate cap – The interest rate for each individual loan, at the time of obligation, may not exceed the National Credit Union Administration's (NCUA) interest rate ceiling for loans made by federal credit unions as described in 12 U.S.C. § 1757(5)(A)(vi)(I) and set by the NCUA board. The NCUA's permissible interest rate ceiling supports its mission to protect credit unions and its consumers. In choosing to adopt the NCUA interest rate ceiling, Treasury aims to ensure that small businesses that participate in SSBCI receive loans that are economically beneficial to them. *(Treasury Guidelines page 44)*
- Fees and Terms – SSBCI-supported transactions may not include:
    1) Confessions of judgment;
    2) Pre-payment or double-dipping fees; or
    3) Upfront fees or charges paid by the small business, excluding fees to the state program, that exceed 3 percent for loans greater than $25,000 or $750 for loans under $25,000
        - Upfront fees or charges that count toward this cap include, but are not limited to, application fees, origination fees, and document preparation fees.

  (Treasury Guidelines page 44-45)

- Disclosure of Terms – SSBCI-supported transactions must include disclosure by the lender of all key terms in an easy-to understand manner including, but not limited to, loan/investment amount; payment obligation/schedule; terms providing control over cash balances, cash flows, or ownership; conversion rights; future rights to purchase equity; and any fees or extra costs. *(Treasury Guidelines page 45)*

14. Loans for Refinancing

(Treasury Guidelines pages 24-25)

A. New Lenders

Under the SSBCI statute, a lender is not prohibited from enrolling or refinancing loans previously made by another, non-affiliated financial institution. However, the purpose of SSBCI is to support small businesses by providing new capital. Accordingly, a lender may refinance a borrower's existing loan, line of credit, extension of credit, or other debt originally made by an unaffiliated so long as the proceeds of the transaction are not used to finance an extraordinary dividend or other distribution.

When a participating state uses SSBCI funds to support the purchase of a loan from another, non-affiliated financial institution, the state must make a determination that the transaction is beneficial to the small business borrower. For purposes of the eligible business purpose and certification requirements, the eligible business purpose of the new loan is generally determined by the purpose of the underlying funding being refinanced.

B. Existing Lenders

A financial institution lender may use SSBCI funds to support a new extension of credit that repays the amount due on a "matured loan" or other debt that was previously used for an eligible business purpose when all the following conditions are met:

- The amount of the new loan or other debt is at least 150 percent of the outstanding amount of the matured loan or other debt;
- The new credit supported with SSBCI funding is based on a new underwriting of the small business's ability to repay the loan and a new approval by the lender;
- The prior loan or other debt has been paid as agreed and the borrower was not in default of any financial covenants under the loan or debt for at least the previous 36 months (or since origination, if shorter); and
- Proceeds of the transaction are not used to finance an extraordinary dividend or other distribution.

If a participating state enrolls a loan that is used to repay principal under a loan previously made by the same financial institution or its affiliate, the participating state or the financial institution lender must maintain records showing that these criteria were met. The limitation on refinancing does not prohibit a financial institution lender from originating a new loan under an SSBCI approved program and subsequently refinancing the same loan under any approved program.

"Matured Loan": A matured loan or line of credit only includes such that have matured according to their terms and does not include a loan or line of credit that has been accelerated to maturity. Transferring an accelerated loan into an SSBCI program does

not promote the purpose of expanding small business access to capital and would primarily benefit lenders rather than small businesses.
(Treasury Guidelines page 24)

15. Ineligible Loans

- Loans to borrowers with 750 or more employees *(Treasury)*
- Loans to finance a non-business purpose *(Treasury)*
- Loans to acquire or hold passive investments in real estate (not owner-occupied) *(Treasury)*
- Loans for land development or speculative ventures *(Treasury)*
- Loans to finance goodwill or blue-sky *(Treasury)*
- Loans to repay delinquent federal or state income taxes unless the borrower has a payment plan in place with the relevant taxing authority *(Treasury)*
- Loans to repay taxes held in trust or escrow (e.g., payroll or sales taxes) *(Treasury)*
- Loans to reimburse funds owed to any owner, including any equity investment or investment of capital for the business' continuance *(Treasury)*
- Loans to purchase any portion of the ownership interest of any owner of the business, except for the purchase of an interest in an employee stock ownership plan qualifying under section 401 of Internal Revenue Code, worker cooperative, or related vehicle, provided that the transaction results in the employee stock ownership plan or other employee-owned entity holding a majority interest (on a fully diluted basis) in the business* *(Treasury)*
- Loans classified as substandard, doubtful, loss or similar category in lender's most recent examination report
- Loans classified as watch, substandard, doubtful, loss or similar category on the lender's internal watch list
- Loans to businesses with classified loans at the lender, other than the loan offered to the CDFI/RLF
- Loans to businesses or individuals with a negative net worth
- Loans for revolving lines of credit

(Treasury Guidelines pages 18-21)
**The tangible assets of an existing business can be purchased using SSBCI proceeds.*

16. Ineligible Borrowers

- An executive officer, director, or principal shareholder of the financial institution lender *(Treasury)*
- A member of the immediate family of an executive officer, director, or principal shareholder of the financial institution lender *(Treasury)*
- A related interest of immediate family member of such an executive officer, director, or principal shareholder of the financial institution lender *(Treasury)*
- State-regulated charitable, religious, or other non-profit or philanthropic institutions; government-owned corporation; consumer and marketing cooperatives; and faith-based organizations, unless the project is for a "business purpose" *(Treasury)*
- A business engaged in speculative activities that profit from fluctuations in price, such as wildcatting for oil and dealing in commodities futures, unless those

activities are incidental to the regular activities of the business and part of a legitimate risk management strategy to guard against price fluctuations related to the regular activities of the business or through the normal course of trade *(Treasury)*
- A business that earns more than half of its annual net revenue from lending activities, unless the business is (1) a CDFI that is not a depository institution or a bank holding company, or (2) a Tribal enterprise lender that is not a depository institution or a bank holding company *(Treasury)*
- A business engaged in pyramid sales, where a participant's primary incentive is based on the sales made by an ever-increasing number of participants *(Treasury)*
- A business engaged in activities that are prohibited by federal law or, if permitted by federal law, applicable law in the jurisdiction where the business is located or conducted (this includes businesses that make, sell, service, or distribute products or services used in conjunction with illegal activity, unless such use can be shown to be completely outside of the business' intended market); this category of businesses includes direct and indirect marijuana businesses, as defined in SBA Standard Operating Procedure 50 10 6 *(Treasury)*
- A business deriving more than one-third of gross annual revenue from legal gambling activities, unless the business is a Tribal SSBCI participant, in which case the Tribal SSBCI participant is prohibited from using SSBCI funds for gaming activities, but is not restricted from using SSBCI funds for non-gaming activities merely due to an organizational tie to a gaming business *(Treasury)*

(Treasury Guidelines pages 18-23)

17. Program Specific Requirements

- All MT SSBCI 2.0 LPP applications must comply with the US Department of the Treasury's SSBCI 2.0 guidelines, Frequently Asked Questions (FAQs), and any changes or amendments that may follow
- MT SSBCI 2.0 LPP funds can be used for non-passive real estate investment construction financing through the CDFI/RLF.
- MT SSBCI 2.0 LPP can participate through the CDFI/RLF in the non-passive real estate investment term loan, the proceeds of which would be used to pay off the construction loan.
- A real estate investment is NOT considered passive if the Borrower occupies 60%+ of the total rentable property following issuance of an occupancy permit or other similar authorization for the construction of a new building or 51%+ of the total rentable property within 12 months following the acquisition, renovation, or reconstruction of an existing building. *(Treasury Guideline page 19)*

- The following statement <u>must</u> appear in either the lender's Note or the Loan Agreement: **"The borrower agrees that as a result of using MT SSBCI 2.0 LPP funds it will provide the lender and/or the MT SSBCI 2.0 LPP with tracking data as required by the US Department of the Treasury. This reporting requirement expires December 31, 2030."**
- Certifications (templates provided by MT SSBCI 2.0)
    - Borrower Use of Proceeds and Conflict of Interest Certification
    - Borrower Sex Offender Certification

- Borrower Certification Related to Business Enterprises Owned and Controlled by Socially and Economically Disadvantaged Individuals (SEDI-Owned Businesses)
- Lender Use of Proceeds and Conflict of Interest Certification
- Lender Sex Offender Certification
- CDFI/RLF Sex Offender Certification

(Treasury Guidelines pages 17-25)

- CDFI/RLF Use of Proceeds and Conflict of Interest Certification

18. Other Loan Policy Considerations

- "Approved Lenders" must have an executed MT SSBCI 2.0 LPP Lender Loan Servicing Agreement and are required to adhere to the terms and conditions contained therein.
- The CDFI/RLF must have a current executed MT SSBCI 2.0 LPP CDFI/RLF Loan Servicing Agreement and must adhere to the terms and conditions contained therein.
- Agricultural loans for machinery and equipment and/or real estate are eligible
- Environmental risk assessment as required by the lender
- Escrow impounds as required by the lender for taxes, hazard insurance, and/or maintenance
- Loans considered by the MT SSBCI 2.0 LPP must comply with lender and CDFI/RLF loan policies
- The participated portion of a MT SSBCI 2.0 LPP funded loan <u>cannot</u> be assigned
- Lenders and CDFI/RLFs are required to submit various data as requested by the state and/or federal government under the MT SSBCI 2.0 LPP
- Anytime a lender downgrades a MT SSBCI 2.0 LPP loan, the lender <u>must</u> notify the CDFI/RLF of the downgrade. Notification must occur within 30 days of the credit downgrade and provide an explanation as to why the credit was downgraded.
- The MT SSBCI 2.0 LPP supported loan must close within 180 days of application date unless extended by MT SSBCI 2.0 LPP for a period not to exceed an additional 180 days from the date of request.

19. Applications/Commitments

- Information for application to the MT SSBCI 2.0 LPP, provided however the recipient submits information deemed confidential pursuant to Montana law, the application and information is deemed a public record.
- Completed loan applications submitted to the CDFI/RLF requesting MT SSBCI 2.0 participation in a new loan with a lender must be signed and include all the required financial information
- Loan applications must include signed proof (i.e., loan committee minutes, lender certification of approval, etc.) of official approval by the lender and the CDFI/RLF
- All completed applications will be reviewed for program compliance by MT SSBCI 2.0 LPP staff

- Upon approval by the MT SSBCI 2.0 LPP, a commitment letter will be issued to the CDFI/RLF listing the terms and conditions that must be complied with by the lender and CDFI/RLF before the loan can be funded
- The review and acceptance of all loan documents or documents required does not constitute the concurrence by the MT SSBCI 2.0 LPP of the accuracy, validity or legality of the documents presented

20. Funding

- Documents required in the commitment letter must be received by the CDFI/RLF prior to funding the loan
- The CDFI/RLF must submit a letter to the MT SSBCI 2.0 LPP requesting release of the MT SSBCI 2.0 LPP funds. The letter must certify that all conditions of the commitment letter have been complied with and copies of all documents required in Schedule A of the commitment letter must be submitted with the letter.
- After the CDFI/RLF funds the participation with the lender, the CDFI/RLF must send a copy of the completed and signed participation certificate to the MT SSBCI 2.0 LPP.

21. Definitions

Approved Lender

To qualify as an Approved Lender for the MT SSBCI 2.0 LPP, a financial institution must have a current executed MT SSBCI 2.0 LPP Lender Loan Servicing Agreement and must adhere to the terms and conditions contained therein when servicing any loans under the MT SSBCI 2.0 LPP.

CDFI/RLF

An economic development organization that is a certified Community Development Financial Institution and/or manages revolving loan funds (CDFI/RLF) that is authorized to access the MT SSBCI 2.0 LPP funds to participate in a small business loan.

Very Small Business (VSB) *(Treasury Guidelines page 12-13)*

A business with fewer than 10 employees at the time of the loan and may include independent contractors and sole proprietors.

Socially and economically-disadvantaged individual (SEDI) owned businesses *(Treasury Guidelines pages 8-12)*

SEDI-owned business needs are being met when MT SSBCI 2.0 funds are expended for loans to:

- Business enterprises which certify that they are owned and controlled by individuals who have had their access to credit on reasonable terms diminished as compared to others in comparable economic circumstances, due to their:
    1) Membership of a group that has been subjected to racial or ethnic prejudice or cultural bias within American society,
    2) Gender,
    3) Veteran status,
    4) Limited English proficiency,

5) Physical handicap,
6) Long-term residence in an environment isolated from the mainstream of American society,
7) Membership of a federally or state-recognized Indian Tribe,
8) Long-term residence in a rural community,
9) Residence in a U.S. territory
10) Residence in a community undergoing economic transitions (including communities impacted by the shift towards a net-zero economy or deindustrialization), or
11) Membership of another “underserved community” as defined in Executive Order 13985

- Business enterprises which certify that they are owned and controlled by individuals whose residences are in CDFI Investment Areas;
- Business enterprises which certify that they will operate a location in a CDFI Investment Area;
- Business enterprises that are located in a CDFI Investment Area

<u>Community Development Financial Institution (CDFI) Investment Area</u>
A geographic unit (or contiguous geographic units), such as a census tract, located within the United States, that meets established criteria. Please contact MT SSBCI 2.0 LPP staff if you would like to confirm if your project is in a CDFI Investment Area.