The Headwaters Fund

INVESTING IN OUR COMMUNITY

Revolving Loan Fund Lender Manual

REVISED APRIL 28, 2020

TABLE OF CONTENTS

1. Introduction and Summary

a) This Manual guides Lenders in administering the Headwaters Fund Revolving Loan Fund with revisions made to reflect the temporary Business Resiliency Emergency Loan Program in response to the Covid-19 disaster declaration.

b) As part of the Loan Fund, the "Lender" (a qualified, Headwaters Fund-approved financial lending institution) markets, underwrites, and services loans for the purpose of job creation and economic development in Humboldt County. Loan Fund loans are designed to provide gap financing in conjunction with commercial lenders or alone. Lenders apply for and are assigned a Loan Pool (the maximum total disbursement for loans) from which they draw to make loans. Funds from the Loan Pool are disbursed on a loan-by-loan basis as needed. For the purpose of the Business Resiliency Emergency Loan Fund (BRELF) only, funds may be advanced to Lender, and borrower's payments may be retained by Lender and revolved until notified by the Headwaters Fund Executive Director to make payments and return payments promptly to the Headwaters Fund. Lenders must approve and structure loans according to the criteria outlined in this document, the Master Participation Agreement (see Section 1c), and the Participation Certificate (see Section 1c). The Lenders must match 1:2 the amount the Headwaters Fund provides for the loan (1/3 Lender to 2/3 HWF) with the exception of loans made under the US Small Business Administration (SBA) Paycheck Protection Program or other SBA Programs that provide 100% guarantees; additional portions of the total loan may or may not come from commercial lenders. If the Lender is unable to provide matching funds for the loan, it may be required to seek final approval for the loan from the Headwaters Fund. The Headwaters Fund will compensate Lenders for costs related to lending as specified in the Lender Agreement, Master Participation Agreement, and Participation Certificate (see Section 1c for description of these documents). The initial term of the relationship between the Loan Fund and the Lender is expected to be about 1-3 years (subject to negotiation) with renewal terms possible.

c) This Manual (or "Lender Manual") along with the Lender Agreement, Master Participation Agreement, and Participation Certificate are the legal documents governing the Lender's relationship, duties, compensation, and rights as part of the Headwaters Revolving Loan Fund Program.

   i) The Lender Agreement outlines disbursements to Lenders from the County, the Lender's lending responsibilities, terms and consequences for an Agreement Default, suspension and termination of the Lender Agreement, and other legal provisions.

   ii) The Master Participation Agreement chiefly outlines the mechanism (i.e. sale of an interest of a Lender loan to the County) for the Lender to match County funds to make loans as well as loan administration requirements, especially for troubled loans.

   iii) The Participation Certificate must be completed by Lender and County for each Headwaters Loan. The Certificate primarily specifies loan terms, compensation to Lender to cover underwriting and administration costs, and collateral recovery arrangements.

2. Definitions

a) "Lender" means a qualified lender approved by the Headwaters Fund to administer Headwaters Fund money.

b) "HWF" means the Headwaters Fund program of the County of Humboldt.

c) "HFB" means the Headwaters Fund Board.

d) “County” means the County of Humboldt.

e) “Board of Supervisors” means the Board of Supervisors of the County of Humboldt.

f) “RLF” means the Headwaters Fund Revolving Loan Fund Program.

g) “HWF/Lender Portion” refers to the amount of a loan provided by either HWF or Lender funds. Commercial bank, borrower injection, and other sources of funds are not included in this amount.

h) “Lender participation” refers to loan funds not from HWF provided by Lender as part of an HWF loan. For example, if there is 40% Lender participation in a loan with an HWF/Lender Portion of $100,000, the Lender provides $40,000 for the loan from non-HWF sources; HWF provides $60,000 for the loan.

i) “Delinquent loan” is a loan where scheduled or required payments are up to 90 days past the original due date.

j) “Default loan” is a loan where scheduled or required payments are over 90 days past the original due date.

k) “Loan loss rate” or “loss rate” for the Lender’s Headwaters Fund Loan portfolio means the total unrecoverable amount of Lender’s outstanding Headwaters loans as a percentage of Lender’s total Headwaters loan portfolio’s outstanding principal amount.

l) A loan “write-off” or “charge-off” means the amount of an outstanding loan expected to be unrecoverable.

m) “Lender Agreement” is the separate document between the Lender and the County of Humboldt outlining disbursements to Lenders from the County, the Lender’s lending responsibilities, terms and consequences for an Agreement Default, suspension and termination of the Lender Agreement, and other legal provisions.

n) “Master Participation Agreement” is the separate document chiefly outlining the mechanism (i.e. sale of an interest of a Lender loan to the County) for the Lender to match County funds to make loans as well as loan administration requirements, especially for troubled loans.

o) “Participation Certificate” is the separate document specifying loan terms, compensation to Lender to cover underwriting and administration costs, and collateral recovery arrangements. The Participation Certificate must be completed by Lender and County for each Headwaters Loan.

p) “Business Relief Emergency Loan Fund” or BRELF is a short-term programmatic revision to the HWF RLF Program in response to the COVID-19 pandemic and its broad economic consequences. The BRELF’s goal is to quickly provide funds to affected Humboldt County businesses with as much flexibility as possible, and responsibly, to improve the County’s economic outlook in wake of the COVID-19 pandemic.

3. Loan Screening and Administration Process

a) Marketing of Loan Products: The Lender will effectively market HWF loan products to qualified organizations by targeting appropriate customer segments, advertising, distributing marketing and application materials, and responding to potential applicant inquiries. At its discretion, HWF staff will work with Lenders to design and implement marketing programs.

b) Loan Application: Applicants apply to the Lender directly for loans. The Lender will assist loan applicants in completing the necessary application materials. The Lender can use its own application forms and procedures, as long as it collects the information required for reports to HWF staff (outlined in Section 14 ‘Reporting & Monitoring’).

c) Loan Evaluation

   i) The Lender will perform a sufficiently detailed and comprehensive analysis of each application to make a reasonable, informed, and responsible loan evaluation decision consistent with industry standards.

ii) The Lender will have its Loan Committee review and recommend for approval all HWF loans. Loan Committee members must have sufficient knowledge and experience in finance, banking, accounting and law to evaluate HWF loans. For the loans originated under the BRELF, the Loan Committee may delegate this authority to Lender's Executive Director and staff.

iii) The Lender will prepare all necessary loan documents and supporting information including Loan Committee recommendations on the appropriateness of each loan.

iv) Other interviews, screening, financial evaluation and analysis are conducted per Lender's usual policies.

v) Loan eligibility and uses must fit Section 4 'Loan Guidelines' below.

d) HWF Input & Approval

i) HWF representative on Lender loan committee: HWF staff and/or HFB have the option to send one representative to sit on the Lender's Loan Committee, subject to that representative signing and complying with any conflict of interest policies of Lender. This representative would have all the duties and authority of normal Lender Loan Committee members.

ii) Exceptions to loan guidelines (specifically outlined in Section 4 'Loan Guidelines') must be submitted to and approved by HWF staff and/or HFB in writing.

iii) Under the RLF, Lender cannot be required to approve a particular loan, but HWF staff and/or HFB may decline to fund/participate in an approved loan under conditions outlined in Section 7 'Lender Participation'.

iv) If HWF approval is required for a loan, Lender must provide HWF staff with appropriate documents (see Section 7g).

v) HWF staff will review all loans to ensure that proposed uses are consistent with HWF policies.

e) Loan Closing & Disbursement

i) The Lender must execute all necessary loan documents.

ii) The Lender must adhere to its customary policies and any agreements of HWF.

f) Appeals Process

i) The Lender must have an HWF staff approved appeals process.

g) Loan Servicing & Monitoring

i) The Lender must monitor project for compliance with loan documents and requirements.

ii) Notice of Payment due dates must be sent to borrowers at least 15 days prior to due date.

iii) The Lender must monitor loans according to its policies and as needed to fulfill HWF reporting & monitoring requirements (outlined in Section 14 'Reporting & Monitoring' and Section 6 'Troubled Loan Guidelines' sections).

iv) Payments from borrowers must be transferred to HWF according to policies in Section 10 "Financial Management and Payment".

v) Troubled loan guidelines are outlined in Section 6.

4. Loan Guidelines

a) The Lender must abide by these guidelines. As long as RLF guidelines are met, the Lender may set loan parameters according to Lender's established policies and judgment. Exceptions to guidelines are specifically noted below and require final approval in writing from HWF staff and/or HFB. In considering exceptional cases, HWF staff may request from the Lender the 'loan report' documents/information outlined in Section 7g.

b) Eligible Organizations

i) Businesses (including start-ups) and non-profit organizations located in Humboldt County. Organization may be located outside of the County if the Extraordinary Project criteria in section 17 are met.

c) Ineligible Organizations

i) Speculative organizations (firms deriving profit from fluctuations in price rather than through the normal course of trade), lending organizations (e.g. banks), political lobbying organizations, pyramid sales organizations, and organizations involved in illegal activities.

ii) Lender

d) All projects must not be commercially bankable on their own.

i) Lender must verify reasonable documentation of need or gap (e.g. bank rejection letter). To provide useful information for Lender and HWF, a bank rejection letter should also include an explanation for the gap (i.e. reason for denial).

e) Eligible Project Uses of Loan Proceeds:

i) Real estate: purchase (land and building), construction, and rehabilitation

ii) Working capital

iii) Equipment and machinery

iv) Inventory

v) Leases

vi) Business buyouts and startup costs

vii) Product development

viii) Debt refinancing, but only on an exception basis or for the BRELF; typically refinancing must fulfill all of the following conditions:

a) The existing debt must not presently be on reasonable terms. The main test for reasonableness is whether existing cash flow is adequate to cover existing debt;

b) The refinancing must provide a substantial benefit to the organization;

c) There must be at least a 20% improvement to the firm's cash flow compared to the previous debt structure. The comparison does not have to be based on similar methods of amortization;

d) The refinancing must not be made to provide additional funds to distribute to owners/investors. Debt due a principal of the applicant business cannot be refinanced regardless of the principal's ownership percentage; and

e) HWF funds may not be used to put Lender or other investor funds in a more attractive/safer position.

f) Documentation to be provided:

(1) Lender certification in writing and transcript of borrower's account showing that debt to be refinanced is and has been reasonably current for at least the last 36 months, except as a result of the Covid-19 declared disaster. Reasonably current means that borrower has made loan payments on time or with three or fewer late payments; and

(2) When a major part of the loan proceeds is for debt payment, the Lender must fully explain how and why the debt accumulated and justify the need for refinancing.

g) Debt refinancing loans under the BRELF may not be required to meet all of the above criteria, upon HWF approval.

ix) Other uses for loan proceeds (e.g. intellectual property, letters of credit, loan guarantees) are eligible on an exception basis only

f) Social Criteria for Loan Proceeds

i) Job creation/retention: proceeds must lead to job creation or retention. Projects must meet or exceed the job-to-loan ratio of 1 full-time job created/retained per every $35,000 loaned (i.e. the total HWF/Lender Portion). Subject to HWF staff and/or HFB approval on an exception basis only, the Lender can make exceptions to this job creation/retention requirement if Lender deems the organization will generate a sufficiently high total economic value to the County (see "Total Economic Value" Appendix 2); and

ii) Fit with the broad vision outlined in the County's Comprehensive Economic Development Strategy (currently named Prosperity 2018), namely: creation/retention of jobs, contribution to the economic vitality of the region, and enhancement of industry clusters or supporting industries.

g) Ineligible Uses of Loan Proceeds

i) Payments for debt or to investors (except as specified in Section 4.e.viii);

ii) Tax payments (except for BRELF loans, at Lender's discretion);

iii) Exclusively private residential projects (mixed commercial/residential projects may be considered); and

iv) Activities and economic benefits located outside of Humboldt County. Assistance may be withdrawn if the activity is later moved outside of Humboldt County.

h) Allowed Financing Instruments

i) Loans;

ii) A line of credit (LOC) except that a LOC may only be made with the written consent of the HWF Board; and

iii) Loans with Royalty Participation

a) Lender negotiates with Borrower to receive a percentage of sales for a future period or above a specified threshold (typically used to compensate for higher risk deals); typically requires audited sales figures.

b) Lender may not conduct Royalty Participation deals until expressively approved in writing to do so by HWF staff.

c) If HWF staff deems that a Lender does not have the needed expertise in executing loans with royalty participation, staff may require appropriate Lender personnel to undergo suitable training before being able to execute loans with royalty participation.

i) Loan Terms and Conditions: Refer to Figure 1 below and Lender Agreement for loan guidelines:

Figure 1: Terms & Conditions Guidelines for Loan Products

Term/Condition	Guidelines	Notes
Required Investment from Borrower	• At least 10% of project cost, with exceptions, in cash or comparably valued equity • As little as 0% required under BRELF, at Lender's discretion	• Valuation and use of non-cash equity should occur according to Lender's policies
Payment Schedule	• Lender discretion	• Options include interest-only payment period, deferred payment period, variable payment schedule, & balloon payments
Private Sector Lender Participation (Leverage)	• Portfolio-wide ratio: At least $1 from private lender(s) and/or the borrower for every $1 of HWF/Lender Portion • No requirement for BRELF loans	• This ratio is computed over a 12-month period starting after the Lender makes its first HWF loan.
HWF/Lender Portion Size	• Minimum: $25,000; at Lender discretion for BRELF loans; • Maximum (established firms): $800,000 (with exceptions as allowed by the Extraordinary Project criteria in section 17.) • Maximum (start-up firms[1]): $200,000 (with exceptions)	• Total loan size = HWF/Lender Portion + Private lender portion • Min/max contribution of HWF depends on Lender participation percentage
Interest Rate	• See Lender Agreement Section 3.7	
Term Length	• Lender discretion	
Loan Fee	• Set by Lender (see Lender Agreement Section 3.7)	
Prepayment Penalty	• None	
Collateral Requirement	• Fully secured (collateral discounted according to Lender policies), junior position to other debt possible; exceptions also possible	• Possible exception: Debt with Royalty Participation; • Exceptions allowed for loans made under BRELF at at Lender discretion

5. Loan Servicing

a) Lender shall maintain a loan file that includes: Note, Participation Certificate, Loan Agreement/Contract, Loan Application Package, Insurance (if applicable), Loan Committee Report, Disbursements, Guaranties (if applicable), and other needed documents.

[1] See Section 9a for start-up firm definition

b) Lender should maintain a “Tickler” system organized by month (when payments are due) and track borrower due dates for insurance payments, taxes, financial statement updates, guarantor financial statements (if applicable), and Uniform Commercial Code renewal dates (if applicable).

c) Lender should maintain a delinquent and lost loans file - A list of all loans deemed un-collectable or delinquent. Delinquent loan information will include recommendations for action.

6. Troubled Loan Guidelines

Workouts, extensions, collections, write-offs, delinquency, and foreclosures will be determined according to Lender discretion and policies, but should at a minimum include the following procedures:

a) As stated in the Master Participation Agreement Section 3, Lender will confer with HWF staff prior to initiation of loan acceleration or collections proceedings. If Lender participation is less than 50%, Lender must obtain written consent of HWF staff before initiating such proceedings;

b) As stated in the Master Participation Agreement Section 13, Lender must promptly notify HWF staff if there are material changes in the value of the collateral securing the loan;

c) Lender may restructure a loan no more than 3 times. If Lender wishes to restructure a loan more than 3 times, Lender must obtain permission from HWF staff and/or HFB, and HWF staff and Lender must agree upon a plan to address the troubled loan;

d) Lender must notify HWF staff of delinquent and default loans within 10 business days following Lender knowledge of delinquency and default (see Section 14 for further reporting requirements);

e) In the event that loan payments are more than 20 days late, Servicer will call the Borrower and ascertain why the payment is late and get a commitment for payment. The Servicer will maintain a log of all verbal and written communication about the past due payments. Penalty fees can be assessed in compliance with loan documents and state laws;

f) If payment has not been received 30 days after the due date, Lender will follow up with a letter stating the amounts past due and explaining that the borrower is in default. If appropriate, Lender will make a site visit;

g) All payments past due 30 days or more will be reported by Lender to HWF staff in a monthly report (see Appendix for reporting requirements);

h) By the 60th day of a late payment, Lender shall:

    i) Develop an agreed upon payment plan to get the borrower current.

    ii) Double check that all collateral documentation is in place and in order and that all insurances required are in place.

    iii) Report to HWF staff detailing the nature of the problem and make recommendations; and

    iv) Develop a strategy for further action, including:

        a) Loan re-structuring;

        b) Strategy to liquidate the collateral;

        c) Notice of default and the intention to foreclose;

        d) Further forbearance of action based upon certainty of repayment and confidence of operations; and

        e) Sending the loan to the collection agency.

i) Foreclosure Policies

    i) In most instances a straight foreclosure will be viewed as the last option. There are, however, instances when foreclosure is the best option and the only remedy to a deteriorating situation. Lender will consult with HWF staff before initiating foreclosure proceedings;

ii) All foreclosure proceedings and actions should be done in such a way as to provide maximum protection for HWF funds (see Master Participation Agreement Section 3D); and

iii) Collateral liquidations must attempt to cover the cost of the outstanding loan principal, any accrued interest owed to the lenders, and the transaction costs of liquidation (i.e. legal, marketing, Staff time). See Participation Certificate for further details.

7. Lender Loan Participation & HWF Approval

In all cases, HWF staff will review and approve a loan recommended for HWF funding by Lender to determine if the loan is for an appropriate use as defined in this Lender Manual. Further HWF staff review and approval may be required as defined in this section.

a) Case 1: 50% Lender participation

- i) The Lender must provide 50% of the HWF/Lender Portion from its own, non-HWF sources. This participation is designed to increase leverage of HWF funds and provide risk sharing between HWF and Lender. There are two exceptions to this 50% requirement:
  - a) Lender's other fund sources explicitly prohibit using funds for a purpose eligible for HWF funds.
  - b) Lender lacks sufficient cash to contribute 50% of HWF/Lender Portion.
- ii) Responsibility and authority for loan underwriting/approval rests with the Lender (subject to terms in this Manual).

b) Case 2: 30 to 49% Lender participation for loans with HWF/Lender Portion under $100,000

- i) If Lender cannot provide 50% participation for the two exceptions/reasons stated in Case 1, can provide 30-49% of the HWF/Lender Portion from non-HWF sources, and the HWF/Lender Portion is less than $100,000, the Lender has the responsibility and authority for loan underwriting/approval (subject to terms in this Manual).
- ii) Lender must provide HWF staff with reasons (and brief documentation) for less than 50% participation.

c) Case 3: 30 to 49% Lender participation for loans with HWF/Lender Potion of $100,000 or more.

- i) If Lender cannot provide 50% participation for the two exceptions/reasons stated in Case 1, can provide 30-49% of the HWF/Lender Portion from non-HWF sources, and the HWF/Lender Portion is more than $100,000, the Lender may still make the deal but requires approval from HWF.
- ii) Using its normal processes, the Lender will underwrite and recommend approval (if appropriate) to HWF staff. HWF staff and/or HFB will have final authority to approve or decline loans.
- iii) Lender must provide HWF staff with reasons (and brief documentation) for less than 50% participation.

d) Case 4: Less than 30% Lender participation

- i) If Lender can only provide less than 30% participation for HWF/Lender Portion for the two exceptions/reasons stated in Case 1, the Lender may still make the deal but requires approval from HWF staff and/or HFB.
- ii) Using its normal processes, the Lender will underwrite and recommend approval (if appropriate) to HWF staff. HWF staff and/or HFB will have final authority to approve or decline loans.

iii) Lender must provide HWF staff with reasons (and brief documentation) for less than 30% participation.

e) Case 5: For BRELF loans, the minimum match is reduced to 1/3 Lender, 2/3 HWF, without the need for HWF staff approval.

f) HWF staff and HFB may not require Lender to approve a particular loan but may decline to fund/participate in an approved loan under Cases 3 and 4 above, and in all cases if loan is not for an approved use.

g) When Lender requires final approval for a loan from HWF staff and/or HFB (i.e. Cases 3 and 4 above and exceptions to loan guidelines), Lender will submit loan request to HWF staff. HWF staff will respond to Lender request within 10 working days of receipt of request, unless prior arrangement on turnaround time is agreed upon between Lender and HWF staff.

h) Loan Report

i) When Lender requires final approval for a loan from HWF staff and/or HFB (i.e. Cases 3 and 4 above and exceptions to loan guidelines), Lender should review, underwrite, and recommend approval to HWF staff. Lender should provide at least the following information to HWF staff for review:

a) Borrower's name and contact information;
b) Principal/owner's name and contact information;
c) Summary of organization;
d) Summary of the project (e.g. use of funds, budget);
e) Eligibility for HWF funds (e.g. legal structure, job creation/retention/economic impact);
f) Loan terms (amount, interest, term length, equity investment, conditions, etc.);
g) Proposed collateral (descriptions, valuation formula, appraisal (if applicable), final value);
h) Cash flow analysis and coverage (adjusted existing cash flow, projected cash flow). Lender should provide detailed information needed to analyze and adjust cash flow (e.g. depreciation, principal payments, coverage ratio);
i) Guarantors (name, income, net worth);
j) Outline and analysis of financial condition of the organization (spread of historical financial statements, capabilities of management, personal financial statements (if applicable), credit reports (business and personal, if applicable));
k) Participation structure (amount of private lender, HWF, and Lender participation);
l) Explanation for Lender's inability to fully participate in loan (if Lender participation is less than 33%); and
m) Lender recommendation for making the loan listing reasons and any concerns.

8. Conflict of Interest Policy

a) HWF staff must approve the Lender's Conflict of Interest policy. This policy must preclude the involvement of any individual, with interests (personal or financial) in a loan, from exercising influence in any aspect of the loan process. If the Lender does not have a suitable policy, HWF staff will work with the Lender to create one. The Lender's Conflict of Interest Policy must include the following:

i) Lender will, for each proposed loan, inform HWF staff in writing and furnish such additional information as HWF staff may require, as to whether and to what extent Lender or its principal officers or employees, including immediate family, hold any legal or financial interest or influence in the Borrower, or the Borrower or any of its principal officers or employees, including immediate family, holds any legal or financial interest or influence in Lender. In the event that HWF staff determines that a conflict of interest exists, the loan may not be made without HWF staff approval.

ii) Officers or employees of Lender or members of any credit committees of Lender shall be barred from participation in any way on any decision regarding projects which that officer, employee or member has a direct or indirect personal financial interest.

9. Portfolio Management Guidelines

a) The goal of portfolio management is to have a diverse portfolio to minimize overall risk and ensure broad impact. Diversification categories and the diversification of the portfolio will be considered at least annually by HWF staff (see reporting requirement section). Effort should be made to achieve a diversity in investments in the following areas:

   i) Mix of loan and investment products: senior loans, subordinated loans, and royalty participation (if approved by HWF staff);

   ii) Mix of development stage of businesses invested in. The following definitions outline development stages:

      a) Seed/Start-up Stage: firm is in business less than one year, but products or services have not been sold commercially.

      b) First Stage: sales initiated for a short time (less than six months); company is not showing a profit yet.

      c) Second Stage: company has been producing goods and services for more than two years and has growing accounts receivables and inventory. Firm is clearly making progress and may or may not yet be showing a profit.

      d) Growth Stage: established company with increasing sales volume over several years with profits at break-even or positive. Firm is continuing to expand.

      e) Mature Stage: well established company with stable sales and intermittent to consistent profits. Firm is anticipating little growth opportunity.

      f) Declining stage: established company with declining sales and profits, serving shrinking markets.

   iii) Mix of borrowers: non-profits, businesses, real estate, agricultural businesses, etc.;

   iv) Mix of loan terms: loans with short, medium, and longer-term maturities to encourage fund liquidity;

   v) Mix of loan uses: business (working capital, equipment, etc.), real estate, etc.; and

   vi) Mix of risk ratings: loans with varying degrees of risk ranked by a Lender’s risk rating system approved by HWF staff.

b) Loans maximum per borrower group: a particular borrower group may not hold more than $800,000 in total loans from RLF, with exceptions as allowed by the Extraordinary Project criteria in section 17. A borrower group is a group financially related to each other such as subsidiaries, joint ventures, partnerships, jointly owned corporations, or individual(s) with ownership interest in another borrower.

c) Loan payment default and loss rate: The Lender should maintain a reasonable loan payment default and loss rate (which will vary according to lending conditions, economic factors, etc.). An excessively high default rate may be grounds for review, greater HWF staff oversight of the Lender, and/or contract termination (see "Lender Agreement" Sections 5 and 6).

10. Financial Management and Payment

a) Through an RFP process, financial institutions will apply to become HWF Lenders.

b) Loan Pool

- i) A Lender Loan Pool will be established for each Lender. This Lender Loan Pool will be the maximum amount of funds available (less Loan and Liquidity Reserves as described below) to a Lender for making loans. The Lender Loan Pool is expected to be a self-sustaining revolving loan fund, providing ongoing capital for loans and revenue to cover costs of loan operations.
- ii) Board of Supervisors will determine the size of the Loan Pool based on their discretion and the financial institution's request. The Loan Pool will be held and managed by County of Humboldt. The maximum Loan Pool size is $3,500,000; may be increased by approval of HWF Board, staff and the County of Humboldt Board of Supervisors or its designee.
- iii) Subject to the terms of the Lender Agreement, Master Participation Agreement and Participation Certificate, loan payments from borrowers, foreclosure proceeds, and other income generated from loans to borrowers will be returned to their original Lender Loan Pool.
- iv) Capital/Liquidity Reserve
  - a) A Capital Reserve Account of the Revolving Loan Fund will be established in order to retain sufficient earnings from the Revolving Loan Fund to absorb any losses incurred on loans made out of the Fund. Funds will be retained from interest earnings totaling 8% of the outstanding balance of loans from the Revolving Loan Fund Pool and set aside in this account. Loan losses will be charged to the Capital Reserve Account. The Capital Reserve Account is separate from funds allocated to the Revolving Loan Fund. Losses charged to the Capital Reserve account will be reimbursed to the account from future interest earnings on loans outstanding. HWF staff and/or HFB will review the history of losses at least annually and have the right to adjust the anticipated loan loss percentage, currently set at the industry average of 8% of outstanding loan balances.
- v) Funds will be disbursed in periodic installments as the Lender commits to make loans to eligible borrowers, up to the original amount of the Lender Loan Pool. Funds may be advanced prior to loans being issued to borrowers for the purpose of the BRELF; and, the total amount in the Lender Pool will be increased while the BRELF is in place and until such time loans made at the increased amount are repaid and the Lender Loan Pool can be reduced to the amount in place at the time the BRELF is implemented. It is recognized that making the transition back to the current amount at the time the BRELF is implemented, $7,000,000, will require reduction over time as loans are repaid.
- vi) In setting the Lender Loan Pool size, the following criteria will be considered:
  - a) The relative demand for funds from other eligible HWF lenders;
  - b) Whether the applicant serves a geographic area or segment of potential borrowers not served by others; and

c) The number of types of eligible projects under RLF guidelines in the Lender's area.

c) Remuneration to Lender

i) The "Master Participation Agreement" and "Participation Certificate" outline payment structure for Lender in administering HWF loans.

d) Collateral collection for lost loans

i) As described in the Participation Certificate, if an HWF/Lender loan is accelerated and charged-off, net proceeds of collateral received by the Lender will be shared pro rata based on the Lender and County's original percentage of a HWF/Lender loan. For example, on a loan with 50% Lender participation, 50% of the proceeds from collateral recovery will be given to County by Lender.

e) Accounting records

i) Lenders must adhere to standard accounting principles and procedures and utilize adequate internal controls.

ii) Lenders must maintain adequate accounting records and source documentation to substantiate the reporting requirements and guidelines of the HWF. Lenders must retain all records pertinent to expenditures, transactions, and loans for the RLF for a period of 5 years after the termination of the loans funded by HWF. In the event of litigation, claims, audits, negotiations or other actions that involve any of the Lender's records, Lender must retain such records until final action resolving all issues occurs, or the expiration of the five-year period, whichever occurs later.

11. Terms and Conditions of HWF/Lender Relationship

a) Lender Applicant Eligibility: In order to approve an application to become a Lender, HWF staff must determine that the lender, either independently or with the assistance of an advisory board or committee or by contract with appropriate agencies, organizations or individuals:

i) is capable of providing financial assistance to businesses in order to create and protect jobs;

ii) is able to prudently and effectively administer a direct loan fund;

iii) is able to coordinate with other business assistance, employment training and social assistance programs;

iv) has a strategy for the creation and retention of jobs;

v) has an effective business marketing plan;

vi) has enough expert assistance available to it to underwrite, document, service and collect loans and assist its clients; and

vii) can provide funds from other sources to satisfy Lender participation requirements in HWF loans.

b) See Lender Agreement, Master Participation Agreement, and Participation Certificate for further terms of the Lender's contract with HWF.

12. Technical Assistance

a) Process

i) Initial contact & screening

a) At the outset of the loan application process, Lender first determines if a loan applicant has a project with a realistic chance for loan approval. If the Lender believes that technical assistance (TA) is warranted for these eligible applicants, Lender can refer applicants to the TA Provider mutually agreed upon by HWF staff and Lender.

b) TA Provider (e.g. the North Coast Small Business Development Center) should have experience in business plan development, general business counseling, collaborating with local economic development lenders, assisting applicants with applying for and receiving economic development loans, and accessing business assistance specialists.

c) Due to lender liability and other issues, the TA Provider should not be part of the Lender's organization.

ii) Technical assistance assessment

a) TA Provider will assess the technical assistance needs of the applicant and collaborate with the applicant to develop a TA plan. The Lender may also give input into the plan. The plan should consider the needs of the borrower and Lender, the capacity of TA Provider, and the funds available for payment of TA.

iii) Pre-loan approval counseling

a) TA Provider will provide necessary counseling according to its assessment.

iv) Encouraging and enforcing the use of technical assistance

a) The Lender, in consultation with TA Provider, may contractually require the borrower to utilize technical assistance for some period during the life of the loan. If assistance is required, the technical assistance plan should be refined to specify frequency, duration, and general content of consultations. Borrowers reneging on technical assistance agreements during the loan period may face higher interest rates, fees, or even foreclosure, at the Lender's discretion.

b) The Lender may also choose other methods of encouraging and financing TA usage including discounts on loan fees and interest rates, higher interest rates to fund TA, cash deposits from borrowers (refundable after TA), and rebates on loan fees after TA.

v) Post-loan approval counseling

a) Borrower will meet with TA Provider staff or specialists as needed or required by technical assistance plan.

vi) Evaluation of technical assistance

a) Lender and/or HWF staff will regularly evaluate the TA process.

b) Eligible forms of technical assistance

i) Pre-loan approval

a) Business plan preparation;

b) Loan application advice; and

c) General business consulting – accounting, marketing, planning, human resources, operations, finance, legal, etc.

ii) Post-loan approval

a) General business consulting; and

b) Troubleshooting & status checks.

13. Other Requirements

a) All programs and projects funded by the Headwaters Fund will carry the HWF logo or statement in their marketing materials where deemed appropriate by HWF staff.

14. Reporting & Monitoring

a) Loan delinquency and default

i) Lender must notify HWF staff of delinquent and default loans within 10 business days following Lender knowledge of delinquency/default.

- ii) As stated in the Master Participation Agreement Section 13, Lender must promptly notify HWF staff if any of the following occur:
  - a) Any change in the financial condition of the Borrower, or of any co-maker, guarantor or endorser, under the Loan, which may have a material adverse affect upon continuation of payments under the Loan or the Loan's ultimate collectability;
  - b) Any material change in the value of collateral securing the Loan;
  - c) Any change in lien status as affecting the secured collateral;
  - d) Any request by the Borrower, or by any co-maker, guarantor or endorser under the Loan for any change in the terms and conditions of the Loan, or in the terms of any note or notes evidencing the Loan or in any security agreement or instrument securing the Loan;
  - e) Any request by the Borrower, or by any co-maker guarantor or surety under the Loan for the release, substitution or exchange of any collateral securing the Loan;
  - f) Any request of the Borrower, or by any co-maker, guarantor or endorser under the Loan for the release of any personal obligations of any such party under the Loan;
  - g) Any request to the Lender for any change in the terms and conditions of the Loan, or in the terms of any note or notes evidencing the Loan, or in any security agreement or instrument securing the Loan;
  - h) Any request by the Lender for an increase in and/or substitution or exchange of collateral securing the Loan; and
  - i) The occurrence of any other event, which with the passage of time and/or failure to cure, would constitute an event of default under the Loan, or under any note or notes evidencing the Loan, or under any Loan Document and/or security agreement instrument securing the Loan.

b) Periodic Reports
- i) Refer to Appendix 1 for 6-month and monthly reporting requirements.
- ii) HWF staff and HFB may change or streamline reporting requirements at their discretion, based on performance of Lender.

c) Ad hoc discussions between HWF staff and Lender regarding Lender performance, loan status, and other issues will also take place as needed.

d) Site Visits
- i) HWF staff and/or HFB will periodically schedule site visits to review the Lender's operating procedures, monitor progress and evaluate the effectiveness of the RLF in supporting the area's economic adjustment process and strategic objectives. Site visits may include review of individual loan files to evaluate loan decision-making as well as visits/interviews with borrowers (coordinated with Lender).

e) Audit of Lender
- i) Lenders shall cause to be performed an annual audit related to HWF funds for the duration of the RLF. Such audits will be conducted by an independent auditor who meets the general standards specified in generally accepted government auditing standards. At HWF staff discretion, part or all of a Lender's audit for other funders/purposes may substitute for part or all of HWF audit requirements provided the Lender's audit includes an accounting of the HWF funds and HWF loan participation accounts under the control of Lender.
- ii) HWF staff and HFB may audit, inspect, or investigate an RLF Lender and any HWF loan related materials at any time. An audit should take place no more than 12 months after the start of relationship with HWF.

f) RLF Monitoring and Annual Report
   i) HWF Staff and HFB will issue an annual public report detailing fund activities and performance and status.
   ii) RLF will undergo an annual audit.
   iii) HWF Staff will regularly develop financial reports and program reviews to monitor RLF operations and allow for HFB and Board of Supervisor review.

15. Evaluation of Lenders

a) Lenders will be evaluated in absolute performance terms and relative to their own evaluation plan outlined in an organization's application to become an HWF Lender.

b) HWF staff and HFB will evaluate Lenders based on loan fund performance, compliance with HWF guidelines, effectiveness in disbursing financing to the community, overall management competency, ability to work effectively with HWF staff and HFB, and other factors.

16. Changes to Policies and Procedures

a) HWF reserves the right to make changes to this Manual and policies governing Lender use of HWF funds as needed.

b) Typographical, editorial, and other non-material changes in this Manual will be made by HWF Staff.

17. Extraordinary Project Criteria

a) Although ineligible according to Headwaters CIF, Grant Fund, and Revolving Loan Fund criteria, an extraordinary project providing extraordinary economic benefit to Humboldt County may still be eligible for Headwaters Funding. This Extraordinary Project must pass the following levels of approval:
   i) Staff and HFB recommendation; and
   ii) BOS super-majority vote approval (i.e. approval by at least four out of the five Board of Supervisors).

b) Selection criteria:
   i) The project must demonstrate a total economic benefit that significantly exceeds the economic benefit from using twice the amount of funds for the Revolving Loan Fund, CIF, or Grant Fund; whichever of the three Funds that would be appropriate and/or most impacted would be the standard against which to judge the Extraordinary Project. In other words, if the Extraordinary Project requests $1 million, its total economic benefit must exceed using $2 million for Revolving Loan Fund, CIF, or Grant Fund investments;
   ii) The calculation of total economic benefit should include measures such as County-wide direct and indirect job creation/retention, wealth generation, workforce development, and business development; and
   iii) No alternative sources of funding should be readily available.

c) Businesses and non-profit organizations are eligible to apply.

d) Individuals, and political lobbying groups are ineligible for funding.

e) Under no circumstances can the Extraordinary Project include using Headwaters Fund money for general County government funding.

APPENDICES

Appendix 1

Lender Reporting Requirements

6 Month Report

Loans and Payments Summary (breakout for HWF & Lender loan portions as needed)

- Total Loans ($ and #)
- Fully repaid ($ and #)
- Current loans ($ and #)
- Delinquent (<90 days) ($ and #)
- In default (>90 days) ($ and #)
- Total Written Off ($ and #)
- Total Loss ($ and #)

Loan Use

- Real estate, working capital, etc.
- Leverage ratio of portfolio

Social Impacts

- Jobs Created
- Jobs Retained

Borrower Demographics

- Firm Phase ($ loaned to)
  - Startup
  - Expansion
  - Retention
- Firm Industry

Administration

- Any staff turnover last 12 months (position)?
- Loan board members (occupation, race, gender)
- Date of most recent independent audit
- Attach audit (if different from last 6-month report's audit)

Narrative Questions

- Any program/activity plans & changes for future?
- Discuss problems/complaints with loan program?
  - How have they been resolved?
- Any problems in fulfilling plan/obligations to HWF?
- Discuss marketing activities

Status of Loan Pool

Total Loan Pool
Less losses (actual and expected)
Less loan committed, but not disbursed
= Current Loan Pool balance available

Individual Loan Information

- Recipient
  - Name
  - Location
  - SIC/Industry
- Loan Type & Description
  - Direct/Guarantee
  - Loan use (by category)
  - Startup/expansion/retention
- Financing by Source
  - HWF RLF $
  - Other public (for lender match) $
  - Private $
  - New Equity $
  - Total $
- Closing Date & Loan Terms
  - Date closed
  - Term (yrs)
  - Interest rate
  - Total fees
- Loan Status
  - Fully repaid (date)
  - Current as of (date)
  - Delinquent (date)
  - Default (date)
  - Write-off (date)
- Repayment status
  - Principle repaid
  - Interest paid
  - Amount delinquent
  - Amount default
  - Amount written off
- Job impact
  - Pre loan jobs
  - Jobs created
  - Jobs saved

Monthly Reporting Requirements

New Loan Activity

- Number of applications received
- Number of loans closed
- Individual loan information:
  - Identify loans made as part of the BRELF
  - Use of loan (e.g. real estate construction, working capital)
  - Amount of loan:
    - Total loan size
    - Portion of loan from Lender (non-HWF funds)
    - Portion of loan from HWF
    - Portion of loan from commercial lender
  - Changes to existing loans
  - Risk rating
  - Firm industry
  - Firm size
  - Firm growth phase (e.g. startup)

New Delinquencies, Defaults and Losses (note: Lender must notify HWF staff within 10 business days of knowledge of borrower delinquency)

- Borrower name
- Days delinquent/default (see
- Principle balance
- Past due interest
- Total interest and principal past due/lost
- Recoveries from defaulted loans
- Notes/explanation

Appendix 2

Total Economic Value Calculation
Loans made under the BRELF must be separately identified

Total Economic Value Rating	Rating
Direct Job Creation/Retention	<1 FTE per $35k loaned
Sales Outside of Humboldt	$X (or % of total sales)
Indirect Job Creation/Retention	X
Purchases from Local Suppliers	$X
Potential Firm Size	Small/Medium/Large
Expected Growth Rate	Low/Medium/High
Workforce Skills Development Potential	Low/Medium/High
Collaboration Potential with Other Firms	Low/Medium/High
Service to an Underserved Area	Low/Medium/High

Use of Total Economic Value Rating

The goal of the RLF is to assist organizations that will contribute to the overall economic condition of Humboldt County. While job creation/retention is an important measure for economic impact, the success of an organization engenders other beneficial impacts to the economy. Thus, if a potential borrower cannot meet the job creation/retention requirement, the borrower may still be eligible for RLF financing if the borrower is likely to create sufficient Total Economic Value in the County. Approvals for loans to these potential borrowers must occur on an exception basis (i.e. Lender must obtain HWF staff and/or HFB approval for loan and submit justification for waiving the job creation/retention requirement).

The Lender will use this Rating scheme to determine if a potential borrower, otherwise ineligible due to insufficient job creation/retention, should still receive funds due to a sufficient Total Economic Impact. Many of the metrics (e.g. collaboration potential with other firms) are necessarily qualitative.

If the Lender determines that the overall Rating is high enough to merit a job creation/retention requirement waiver, the Lender must submit its Rating (with reasons) to HWF staff as part of the loan documentation.