Brockton Downtown Restaurant Infrastructure Fund

Policy and Procedures Manual

A Program of the Brockton Redevelopment Authority in Partnership with the City of Brockton

Capitalized with the HUD Section 108 Loan Guarantee Program

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Section 1: Mission of the Downtown Restaurant Infrastructure Fund & Service Area:

(A) Mission of the Downtown Restaurant Infrastructure Fund:

The Brockton Downtown Restaurant Infrastructure Fund ("BDRI" or the "Fund") has been created with the intent to establish a funding mechanism to promote the establishment of new, full-service restaurants and dining opportunities in the heart of Brockton's downtown business district. The Fund will be geared toward the creation and promotion of full-service restaurants and will be authorized to make loans to eligible borrowers within the Downtown District. The Brockton Redevelopment Authority ("BRA") will administer the Downtown Restaurant Infrastructure Fund on behalf of the City of Brockton.

(B) Downtown District Geographic Service Area:

Eligibility for funding under the Downtown Restaurant Infrastructure Fund shall be limited to the area encompassing the Downtown Dining District. The Downtown Dining District is located within [INSERT] boundaries are to the North Side of [INSERT] to the North Side of [INSERT] to the South side of [INSERT] to the West to [INSERT].

Section 2: Fund Organization, Lending Authority & Interest Rates:

(A) Fund Organization:

The Downtown Restaurant Infrastructure Fund has been capitalized using the proceeds of a United States Department of Housing and Urban Development ("HUD") Section 108 Loan Guarantee. The Section 108 Loan Program carries with it certain regulatory requirements that mandate certain eligibility criteria be met in order for a Borrower to participate in the program.

Section 108 of the Housing and Community Development Act of 1974 provides for a loan guarantee component of the Community Development Block Grant (CDBG) Program. The Section 108 Loan Guarantee Program (Section 108) provides communities with a source of financing for economic development and can be loan via the City to a third party to undertake the eligible projects. Eligibility for participation in the Section 108 Loan Guarantee program is governed by the regulations found at 24 CFR 570 Subpart M. Given the federal funding source for the Downtown Restaurant Infrastructure Fund requires that the City of Brockton (acting by and through the Brockton Redevelopment Authority) must strictly adhere to the regulatory requirements in administering the loan program.

The Brockton Redevelopment Authority is responsible for Fund oversight and ensuring compliance with applicable HUD regulations.

(B) Lending Authority & Loan Size:

The Downtown Restaurant Infrastructure Fund will be capitalized with $1.5 million in HUD Section 108 Loan Guarantee funds and administered by the City of Brockton's Brockton Development Authority subject to the credit decisions rendered by the Fund Loan Committee (see criteria set forth below under Section 4). Under the Downtown Restaurant Infrastructure Fund program applicants may apply for loans between $50,000 and $350,000 depending upon eligibility, underwriting review, and overall creditworthiness. Pursuant to HUD regulations eligible borrowers are required to create at least one (1) full time equivalent (FTE) job for each increment of $35,000 borrowed under the program.

(C) Applicable Interest Rates & Term of Loan:

(1) **Applicable Interest Rate**:

Interest rates will be determined according to HUD's cost of funds plus an agency spread of 20 basis points on the cost of funds. The HUD rate is calculated as 3-month LIBOR + 20 basis points. The City of Brockton in order to cover the costs of the Loan program may at its sole discretion, charge 100 basis points (or 1%) over HUD's cost of funds. Therefore, loans made to end Borrowers pursuant to the Downtown Restaurant Infrastructure Fund may feature an interest rate that represents 3-month LIBOR plus 120 basis points (1.20%).

The Fund Loan Committee may in its sole discretion, offer to restrict loan payments during the first two (2) years of any loan originated under the Downtown Restaurant Infrastructure Fund program to interest only, with principal payments deferred into the term of the loan. In such scenarios the Borrower would be obligated to pay interest-only during the first two (2) years of the term of the loan.

(2) Term of Loan:

Loans originated under the Downtown Restaurant Infrastructure Fund shall have terms that may range from 5 to 20 years. The DDDF Loan Committee shall retain sole discretion to determine the term of any loan originated under the program and shall make such determinations based upon the relevant credit and collateral considerations presented by an Applicant loan request. In general, the loans created under this program will be self-amortizing but shall in no case exceed a 20-year term.

(3) Types of Loans:

The Downtown Restaurant Infrastructure Fund is authorized to make the loans for fixed assets including furniture fixtures and equipment ("FF&E"), loans for machinery and equipment, construction and build of core restaurant infrastructure and shell space (subject to Davis-Bacon requirements as applicable) and working capital loans. All loans made under the Downtown Restaurant Infrastructure Fund program are fully recourse to the Borrower and must be evidenced by personal guarantees by all individuals owning more than 20% of the business entity.

Section 3: Loan Application, Fees, & Required Documentation

(A) Loan Application:

See Attached Loan Application

(B) Application Fee:

Prospective Applicants to the Fund are required to submit a complete Application (including all attachments) and a non-refundable application fee of $100 made payable to: “Brockton Redevelopment Authority”.

(C) Required Application Documentation:

The Brockton’s Downtown Restaurant Infrastructure Fund is limited to businesses that are or will be located within boundaries of the Downtown Dining District as delineated above in Section 1. Highest consideration will be given to those businesses, which demonstrate that they will create and/or retain the highest number of jobs for low- and moderate-income persons for the least amount of loan Fund assistance. In order to qualify for the Downtown Restaurant Infrastructure Fund program, a business must create and/or retain at least one (1) full time equivalent job (FTE) per each increment of $35,000 of loan proceeds received and at least 51% of those jobs to be created and/or retained must be for low- and moderate-income persons within the meaning provided for at 24 CFR 570.209.

All Applicants to the Downtown Restaurant Infrastructure Fund shall be required to submit to the Fund Loan Committee the following documentation:

- A profit and loss statement for the past three (3) years;
- A personal financial statement for each person holding an ownership interest of more than 20% of applicant business;
- Three (3) years tax returns for the business;
- A cash-flow pro forma that indicates the future needs of the business (featuring a three (3) year projection of the business);
- A narrative description of the project contemplated, including identification of any FF&E and M&E requirements;
- A Sources and Uses statement of the proposed project;
- An estimate of the number of LMI jobs to be created;
- Credit references and contact information;

- A description and documentation of ownership or collateral and its certified market value (i.e. an appraisal conducted by an independent third-party appraiser);

Section 4: Fund Loan Review Committee, Selection, & Approval

(A) Fund Loan Review Committee:

The Brockton Redevelopment Authority will establish a Loan Review Committee comprised of five (5) members. Three (3) members of the Loan Review Committee may be City employees with expertise in financial analysis and/or business credit. The balance of the Loan Review Committee will be comprised of individuals drawn from the community whom are active in banking, financial services experience, insurance or possess other relevant underwriting experience. The Loan Review Committee will play an active role in reviewing applications to determine whether they qualify under the program.

(B) Loan Application Review & Selection Process:

(1) Eligibility Review:

The Loan Review Committee shall be examining the creditworthiness of a particular shall determine that the application conforms to the following eligibility criteria:

1. Determination of Eligibility with Downtown Restaurant Infrastructure Fund Program (e.g. Located within DDDF Area)
2. Proposed project is in conformity HUD Section 108 Requirements specifically:

   i. **Eligible Use/Activity:** as defined at: 24 CFR 570.703
   ii. **National Objective**: as per: 24 CFR 570.208
   iii. **Public Benefit Standards**: as per 24 CFR 570.209

3. Eligible Borrower: The Loan Review Committee according to the criteria set forth in the Underwriting Guidelines contained in Section 5 below;

(2) Underwriting Review: and Financial Risk Analysis:

The Loan Review Committee will conduct the second prong of its review by evaluating applications according to the criteria set forth in **Section 5** below.

(3) Authorized Actions by the Loan Review Committee:

Upon completion of steps (1) and (2) above and the Loan Review Committee having had the opportunity to review the eligibility and creditworthiness of the application before it, the Loan Review Committee may take the following three actions it may:

1. **Contingent Approval**: approve the application subject to further due diligence;
2. **Rejection**: reject the application for any reason enumerated under the Underwriting Guidelines, or
3. **Request for Further Information**: may request the applicant resubmit the application subject to certain contingencies enumerated by Loan Review Committee or for additional information from an applicant Borrower.

In the event that the Loan Review Committee has approved an application according to the criteria set forth in Section 5 below, the Loan Review Committee must make the following certifications as set forth in Section 4(C) below.

(C) Approval & Loan Review Committee Certifications:

In the event that the Loan Review Committee has determined that an application has met all of the required underwriting criteria and has approved the application for further processing, the Loan Review Committee shall sign a statement that the Loan Review Committee has determined in its judgment that following certifications can be made:

(a). The recipient can repay the proposed assistance;
(b). Project costs are reasonable;
(c). All sources of project financing are committed;
(d). The Downtown Restaurant Infrastructure Fund monies are not a substitute for other private non-federal financing;
(e). The project is financially feasible;
(f). The return on the owner’s equity investment will not be unreasonably high; and
(g). To the extent practicable the Downtown Restaurant Infrastructure Fund monies will be disbursed on a pro rata basis with other financial sources provided to the project.

Section 5: Underwriting Policy, Collateral Guidelines & Loan Ratings

(A) Underwriting Policy Generally:

The Applications that the Loan Review Committee will consider must conform to the guidelines of the Downtown Restaurant Infrastructure Fund program. The Applications must be focused on business retention, expansion, or development and all must have emphasis on job creation within the meaning provided for under the HUD Section 108 guidelines. Every prospective application will be subject to an exacting set of underwriting criteria in addition to meeting HUD Section 108 criteria of Eligibility, National Objective, and Public Benefit requirements. In no event shall a loan originated under this program exceed a loan to value ratio of 80%.

In general, the asset being financed will serve as the collateral and in most cases the Loan Review Committee will require 100% collateral coverage. In certain case the Loan Review Committee will subordinate its lien to other financing, provided that in all cases the loan to value ratio of 80% is maintained. The Loan Review Committee shall review applications on a case-by-case basis.

(B) Ineligible Borrowers and Ineligible Activities:

(1) Ineligible Borrowers:

The following types of businesses are ineligible under the Downtown Restaurant Infrastructure Fund program:

- Passive income companies
- Lending and investment institutions
- Unregulated media such as newspapers and magazines
- Speculative ventures
- Charitable organizations
- Employees of the City of Brockton

(2) Ineligible Activities:

The following activities (include but are not limited to) are ineligible for participation under the Downtown Restaurant Infrastructure Fund program:

- A project whereby the requisite amount of job creation in the aggregate would fail to create and/or retain one FTE job for each increment of $35,000 of funds provided

- Reimbursement of project costs prior to submission of an application
- Refinancing of permanent debt (although a business' use of interim financing is permissible)
- Repayment of delinquent taxes
- Product development costs
- General government expenses
- Political activities
- Loans to Borrowers outside the geographic boundaries of the Downtown Restaurant Infrastructure Fund Service Area as delineated in Section 1(B) above.

(C) Collateral Guidelines:

The Loan Review Committee shall not in any case approve an application for funds whereby the City's collateral position is in excess of 80% loan to value inclusive of all other financial sources senior to the Downtown Restaurant Infrastructure Fund loan. In all cases, a prospective borrower must furnish the Loan Review Committee with evidence of sufficient collateral either in the form of an independent third-party appraisal or in such other forms as may customary and common within the banking industry. In no circumstance may the Loan Review Committee deviate from the collateral requirements imposed by the HUD Section 108 loan guarantee program. The Loan Review Committee will evaluate the sufficiency of collateral for Downtown Restaurant Infrastructure Fund loans according to the financial analysis set forth at Section 5(D) below.

(D) Financial Analysis & Credit Rating Determination:

The Fund in conjunction with the Applicant Borrower will assemble the requisite application information while exercising its underwriting responsibilities. The Loan Review Committee will evaluate the creditworthiness of the Applicant based upon a financial analysis of the information presented. The Fund has a three-tiered cash flow Classification system. Class I credits will in all likelihood be approved, Class II credits achieve approval only after a more subjective credit evaluation occurs and Class III credits are only approved with strong alternative first ways out and are limited to 10% of the portfolio. Note that in *all* instances, Cash Flow Classifications on existing companies will be made only based on the last available FULL YEAR Financial Statements (or tax returns) provided. Interim statements will not be used in this assessment, as they do not reflect the impact of a full year's cycle of operations. At underwriting, every loan will receive three separate classifications using the following system based upon a business' existing and historical cash flow:

ADJUSTED CASH FLOW COVERAGE (1)		**DISCOUNTED COLLATERAL COVERAGE (2)**		**ADJUSTED PERSONAL NEW WORTH**		**PAST YEAR'S REPAYMENT RECORD**	
Class	Quality	Class	Quality	Class	Quality	Class	Quality
I.	Existing is equal to or greater than 1.0 : 1	A	1.0 +:1	+	Greater than or equal to DDD Fund loan amount	a	No pmts pmts later than 10th of month
II.	Projected is equal to or greater than 1.0:1	B	.85 to 1.0:1	-	Less than DDD Fund loan amount	b	1 or 2 pmts later than 10th of month
III.	Secondary Source	C	Less than .85:1			c	3 or more pmts later than 10th of month

Classification Category Notes:

- A Cash Flow Classification will be made only based on the last available full year financial statements;
- Class I, II, or III is based on the analysis of adjusted cash flow available for debt service;
- Class A, B or C is based on the analysis of discounted collateral coverage relative to the Downtown Restaurant Infrastructure Fund loan;
- Class + or – is based on the analysis of the guarantor's adjusted personal net worth vis-a-vis the Downtown Restaurant Infrastructure Fund loan amount and
- Class a, b or c is assigned after the loan is booked and based on the timeliness of payments received during the first and all subsequent years.

In order to determine the Class of loan that an applicant falls into, the Downtown Restaurant Infrastructure Fund Loan Review Committee will employ the following three credit tests to determine the creditworthiness of an applicant borrower: **(1) Existing Cash Flow Test, (2) Projected Cash Flow Test, and (3) Collateral Value Credit Test.** Upon completing the review of the preceding underwriting credit tests, the Loan Review Committee will proceed to Section 5(E) below, to evaluate the sufficiency of personal guarantees to be provided by prospective borrowers.

(1) Existing Cash Flow Test (Classified as “Class I” Loans)

The preferred credit test for the Downtown Restaurant Infrastructure Fund would require that an applicant borrower's existing cash flow from operations (after certain adjustments), will be adequate to repay the proposed debt service. Expressed in terms of a formula the credit test can be stated as the following:

ADJUSTED EXISTING CASH FLOW > PROPOSED DEBT SERVICE

The "Adjusted Existing Cash Flow" is determined by adding-in or subtracting-out certain items which are impacted by the proposed financing. It is determined as follows:

ADJUSTED EXISTING CASH FLOW

Last year's Earnings Before Taxes
\+ Depreciation (from Income Statement)
\+ Amortization (from Income Statement)
\+ Interest payments (from Income Statement)
\+ Savings in Rent, Officer Compensation (if applicable), or "Other"
\- Increased Occupancy Costs (occurring as a result of the project being financed)
\- Increased Real Estate Taxes (occurring as a result of the project being financed)
\- Other project related expenses (if any) or Capital Expenses to be paid out of cash flow
= **Adjusted Existing Cash Flow**

In order to determine the amount of "surplus" cash, or the Cash Flow Margin, from the Adjusted Existing Cash Flow, all debt service obligations are subtracted.

<u>Cash Flow Margin</u>

Adjusted Existing Cash Flow
- Existing (Current) Interest and Principal Payments on all non-Fund Debt
- <u>Proposed Project Debt Service (Principal and Interest)</u>

= **Cash Flow Margin** or (Cash Flow Shortfall if negative)

The Existing Cash Flow **Coverage Ratio** is defined as the adjusted existing cash flow divided by the proposed debt service (*principal and interest on both existing and (Downtown Restaurant Infrastructure Fund, project debt*). If the adjusted existing cash flow is greater than the proposed [total] debt service, the coverage ratio will be greater than 1:1, and the borrower and the proposed project will "pass" the cash flow test (and be Classified as a **Class I** deal).

<u>Existing Cash Flow Coverage</u>

Adjusted Existing Cash Flow $\geq$ All Proposed Debt Service

If the adjusted existing cash flow exceeds the proposed debt service and all the evidence and trends suggest that cash flow will continue to exceed the proposed debt service, in all likelihood, the company is "bankable" and the Fund will approve the loan. The credit test demonstrates that the company will have demonstrated that its existing operations throw-off sufficient cash flow to repay the proposed borrowings. The company will not have to rely on any growth or outside sources to repay the proposed obligation. This type borrower receives a "Class I" classification.

If an applicant fails to achieve a "Class I" classification, it does not mean that the borrower is not creditworthy. Rather, it means that in order to repay the proposed obligation, the company's sales must grow, and profits must increase. Failure to grow will mean that the borrower might have difficulty repaying the loan with cash flow from operations in a timely fashion.

To assess the ability of the company to grow and increase profits, the Fund Loan Review Committee will look to the company's projections and to the company's principals. The projected cash flow, based upon a reasonable and achievable projected P&L, must be adequate to repay the proposed debt service. In terms of a formula the credit test for these type companies will be the following:

<u>(2) Projected Cash Flow Test (Classified as "II" Loans)</u>

A borrower request failing to achieve a Class I classification, (but able to satisfy the Fund Loan Committee that its projections are reasonable, and its principals are solid, and its projected cash flow is reasonable and achievable) will receive a Class II designation. In certain events where an applicant falls into a Class II category, it may be upgraded to a Class I by restructuring the proposed financing (e.g. by reducing the project size, changing the maturity of the debt, increasing the equity portion, etc.) so that the existing cash flow becomes sufficient to repay the proposed debt service.

PROJECTED CASH FLOW > PROPOSED DEBT SERVICE

The projected cash flow will be adjusted in a manner similar to the adjustments in the existing cash flow as described above:

<u>PROJECTED EXISTING CASH FLOW</u>

Projected EBT
+ Projected Depreciation (from projected Income Statement)
+ Projected Amortization (from projected Income Statement)
+ Projected Interest payments: on both existing and Fund project loans (from projected Income Statement)
- Any owner’s equity withdrawal (“Off-Income Statement” compensation)
- <u>Any Capital Expenses to be paid out of cash flow</u>
= **Projected Cash Flow**

The Projected Cash Flow must be greater than all of the proposed debt service (principal and interest on both existing and Fund project).

Cash Flow Margin

- Existing Interest and Principal Payments on all Non-Fund Debt
- Proposed (DDD Fund Funded) Project Debt Service (Principal and Interest)
= Cash Flow Margin or (Cash Flow Shortfall if negative)

And the projected cash flow coverage ratio must be greater that the below formula:

Projected Cash Flow Coverage

Projected Cash Flow $\geq$ 1:1 All Proposed Debt Service

Proposed loans that exceed the above ratio are assigned a Class II classification. In applications where existing cash flow is not adequate to repay the proposed debt, in addition to closely assessing the reasonableness and achievability of the projected cash flow, the Fund Loan Committee will more closely scrutinize the capability of the company's principals. The principals must demonstrate adequate organizational skills to be able to generate and manage the necessary growth and to increase the profits to the level at which cash flow will be sufficient to repay the proposed debt. Obviously, in situations where existing cash flow is not adequate to repay the proposed debt, the evaluation of the credit will be more subjective and less objective.

(3) Collateral Value Test (Class III Loans):

If a company fails to receive a Class I or a Class II designation, it will receive a Class III classification. By definition, in Class III companies, existing cash flow or cash flow based upon a reasonable projection will not be sufficient to repay the proposed debt in an orderly fashion. In these cases where cash flow is limited to repay debt, alternative routes for financial structuring may be taken. For example, potential sources of repayment could be standby letters of credit from third parties, outside guarantees, outside income streams, or outside collateral. The collateral of the project and the company cannot serve as an alternate first way out, because it is already being relied upon as the second way out. The Downtown Restaurant Infrastructure Fund will in no event permit more than 10% of its portfolio to be in loans to Class III companies.

Every loan must have two ways of covering losses in the event of a default. The first way out is cash flow. The second way out is collateral. Within reason, the stronger the first way out, the less concerned we need to be about the second way out. In all cases, however, collateral must be adequate to secure the obligation. The Downtown Restaurant Infrastructure Fund will secure a loan with a general security agreement, a perfected lien on all assets, and the personal guarantees of all principals who own 20% or more of the stock and/or play a key role in management. Key person life insurance is also normally required.

Regardless of how strong or weak a company's cash flow appears, the Fund Loan Committee must assess the adequacy of the collateral being offered to secure the loan. Collateral value is not the same as the fair market value of the real or personal property offered as collateral because the time and cost of liquidating the collateral will cause the net proceeds to be less than the hypothetical fair market value of the collateral. For example, real estate is the least liquid of collateral and generates the greatest amount of expenses to hold. For example, if the Downtown Restaurant Infrastructure Fund were obligated to foreclose on a borrower and take real estate as collateral for its loss, then certain additional expenses might arise such as insurance, utilities, taxes, and potential brokerage fees. As such the Downtown Restaurant Infrastructure Fund would seek to avoid to the extent as is practicable foreclosing on mortgages and instead work to find alternative sources to repay defaulted loans.

In the case of machinery and equipment (M&E), foreclosure on M&E normally involves an auction or liquidator who sells the collateral for a price substantially below fair market value in order to liquidate the collateral quickly and to allow for the cost of removal from one site and the installation at another site.

Finally, regarding receivables and inventory, the collateral value of these assets is far less than their cost or face amount because when a company is in trouble, inventory be used by the business to fund other losses or more pressing creditors. For these reasons, determining collateral value is more involved than simply adding up the cost or appraised value of a group of assets.

Downtown Restaurant Infrastructure Fund will look for at least a 1:1 collateral coverage of the loan amount based upon the criteria described below:

<u>Collateral Value Coverage</u>

Collateral Value > 1:1 Loan Amount

Needless to say, the Fund Loan Committee is neither inflexible in its interpretation of collateral value nor rigid in its insistence on a 1:1 coverage. In much the same process as with the evaluation of cash flow, Fund utilizes a three tier Classification system based on a "discounted" valuation of collateral.

The following are the guidelines the Fund Loan Review Committee uses in assessing collateral value:

<u>COMMERCIAL REAL ESTATE: 75% of Value</u>

If Downtown Restaurant Infrastructure Fund receives a first lien on a piece of commercial property, the collateral value of the property will be 75% of the fair market value of the property as determined by an objective and independent outside appraisal. If the Fund takes a mortgage on a piece of property on which there are one or more preceding liens, the collateral value of the property will be 75% of the fair market value of the property, less the amount of preceding liens <u>provided</u> the preceding liens encumber less than 40% of the fair market value of the property.

If the preceding liens encumber more than 40% of the fair market value of the property, the collateral value of that piece of property will be assumed to be zero. This assumption of zero value is because to realize the value of the subordinated mortgage, the Fund would have to make a substantial payment to the first mortgage holder to satisfy that lien. The Fund may not have the resources at the time of foreclosure to satisfy a substantial first mortgage lien, and thus is unable to count the unencumbered portion of the property's value when the preceding liens are significant (i.e. over 40%). In these situations, if the terms on the existing mortgage debt are draining the company's cash flow, it may make sense to repay (refinance) the first mortgage with the Fund loan proceeds in order to provide cash flow benefit to the small business and secure a first lien position.

RESIDENTIAL REAL ESTATE: 80% of Value

If the Fund receives a first lien on a piece of residential property, the collateral value of that piece of property will be 80% of the fair market value of that piece of property as determined by an objective and independent, outside appraisal. If the Fund takes a mortgage on a piece of residential property on which there are preceding liens, the collateral value of the property will be 80% of the fair market value of the property, less the amount of the preceding liens, provided they encumbers less than 60% of the fair market value of the property.

If the preceding liens encumber more than 60% of the fair market value of the property, the collateral value of that piece of property will be assumed to be zero for the same reasons described above under commercial real estate.

VACANT LAND: 50% of Value

If the Fund receives a first lien on a piece of vacant property, the collateral value of that piece of property will be 50% of the fair market value of that piece of property as determined by an independent, outside appraisal. If the Fund takes a mortgage on a piece of vacant property on which there are preceding liens, the collateral value of the property will be assumed to be zero for the same reasons described above under commercial real estate.

MACHINERY AND EQUIPMENT: 50% of Value

If the Fund receives a first lien on a piece of machinery and equipment (M&E), the collateral value of that piece of M&E will be 50% of the fair market value of the M&E. Fair market value can be determined either through independent appraisal or through an estimate from a reputable equipment dealer who opines as to the economic life of the asset, the cost new, and the value of the specific piece of equipment being offered as collateral. If the M&E has preceding liens, the collateral value of the M&E is assumed to be zero. In situations where there are preceding liens on a piece of M&E, it may make sense to satisfy (refinance) them with the Fund loan proceeds in order to obtain a first lien position.

This discussion relates to “heavy” equipment and production equipment. In certain instances, and at the sole discretion of the Fund, fixtures, and light equipment (office, computer, restaurant, etc.) may be valued for collateral analysis purposes at less than 50% of FMV.

INVENTORY AND RECEIVABLES: 20% of Value

From a collateral value perspective, term loans for working capital are completely different than asset-based lending. Asset based lenders normally accord receivables a collateral value equal to 80% of the face amount of the receivables (less than 90 days old) and inventory a collateral value equal to 50% of cost. Asset based lenders are able to accord such high collateral values to inventory and receivables because they monitor receivables and inventory on a monthly basis, tracking receivables by individual invoices and counting inventory, piece by piece. Term lenders on the other hand, secure inventory and receivables by perfecting liens through a general security agreement. Should a borrower get into trouble, the entrepreneur retains full control of the inventory and receivables and uses them in the manner he/she sees fit until foreclosure proceedings are begun. Not surprisingly, inventory and receivables "disappear." In reality, inventory is simply sold and receivables are collected and used to fund losses or satisfy more pressing creditors (e.g. the inventory supplier who is threatening to stop shipments, an insurance company who is threatening to cancel necessary coverage, the IRS who is threatening seizure, or employees who have to be paid at the end of the week). Thus, the collateral value of inventory and receivables to a term lender such as the Downtown Restaurant Infrastructure Fund is highly suspect. In spite of this fact, for valuation purposes the Fund will accord to inventory and receivables, a collateral value equal to 20% of the face amount of not liened inventory and receivables.

The discounted value of all of the collateral being pledged to secure the loan will be added together and classified A, B or C, as previously described.

(E) Downtown Restaurant Infrastructure Fund’s Personal Guarantee Policies

All Downtown Restaurant Infrastructure Fund loans require the personal guarantees of every owner of 20% or more of the company stock, it is a requirement of the HUD Section 108 regulations. In some instances, the guarantees of non-owner key management are also required. In general, the guarantees are "unlimited" (i.e. guaranteeing full repayment of the loan, irrespective of percentage of ownership or personal net worth).

The third component of the Downtown Restaurant Infrastructure Fund Classification System relates to the net worth of the principals who are pledging their personal guarantee to repay the Downtown Restaurant Infrastructure Fund loan. Based on the information provided by the guarantors for the loan, the Downtown Restaurant Infrastructure Fund will discount the assessment of assets and subtract all existing personal liabilities in order to reach an "Adjusted Net Worth" figure. Those discounts are as follows:

PERSONAL ASSET	DISCOUNTED %
Cash and Savings Accounts	0%
IRA or other Retirement Accounts (if they can be pledged or borrowed against, otherwise they are discounted 100%)	50%
Unqualified and substantiated A/R and N/R (from other than the SBC)	100%
Life Insurance CSV	0%
Real Estate (less all liens)	20-25%
Automobile and Other Personal Property	80%
Unqualified "Other Assets"	100%

From discounted value of the personal assets, the face amount of *all* existing and contingent liabilities is subtracted in order to calculate an Adjusted Net Worth.

<u>**Adequate Adjusted Net Worth ("+" Class)**</u>

Adjusted Net Worth < DDD Fund Loan Amount

In those instances where the combined Adjusted Net Worth of the guarantors is greater than the Downtown Restaurant Infrastructure Fund loan amount, that loan will be accorded a "+" classification.

<u>***Insubstantial Adjusted Net Worth ("-" Class)***</u>

DDD Fund Loan Amount < Adjusted Net Worth

In those instances where the combined Adjusted Net Worth of the guarantors is less than the Downtown Restaurant Infrastructure Fund loan amount, that loan will be accorded a "-" classification. A strong Class IA+ or Class IB+ deal which is otherwise eligible stands a very good chance of being approved as submitted.

Section 6: Loan Closing Procedures:

(A) Loan Closing Generally:

Once the Loan Review Committee has performed its review of an application and has determined that the application to be creditworthy, the Loan Review Committee will cause to be issued a Conditional Term Sheet and Commitment Letter. Upon the event that the Term Sheet is deemed acceptable to the Borrower staff from the Brockton Redevelopment Authority will make provisions for closing the loan with the Borrower and HUD. Among the closing documents that the Borrower will be obligated to execute, will at a minimum include the following:

- Promissory Note executed in favor of the City of Brockton or the Brockton Redevelopment Authority
- Contract for the Loan and Note (HUD Document)
- Unlimited Unconditional Personal Guarantee (HUD Document)
- Commitment Letter and Term Sheet
- Loan & Security Agreement (HUD Document)
- Principal and Interest Repayment Schedule
- Custodial Document Agreement with Local Financial Institution

Once the above documents have been executed, BRA Staff will forward the completed Loan Package to HUD's Boston Field Office for review. Upon determining the sufficiency of the Loan Package, HUD's Boston Field Office will advance the package to HUD's Washington Headquarters for approval and release of funds. Once HUD Washington has released the requested funds to the custody of the City of Brockton, the BRA and Borrower will conduct a financial closing of the transaction at mutually agreeable time and place.

(B) Collateral Securitization:

All Loans made pursuant to the Downtown Restaurant Infrastructure Fund are subject to the mandatory underwriting standard requiring an 80% loan-to-value ratio on all loans made. All Borrowers must provide sufficient documentation of collateral to substantiate the required 80% underwriting ratio. Sufficient documentation may include an appraisal performed by an independent third party or such other documentation as is usual and customary within the lending industry. In the case of loans made for fixed assets, machinery and equipment (M&E), and furniture fixtures and equipment (FF&#) and other tangible items, the City or BRA will maintain a UCC Article 9 security filing with the Massachusetts Secretary of State. The

Borrower shall be obligated to provide the City or BRA Staff with all information as may be necessary for the City or BRA to perfect its UCC filing. In the case loans made for real property improvements, the City shall perfect a mortgage lien as against the premises financed and shall record the same in the Registry of Deeds for Plymouth County.

In all cases, the City shall on an annual basis ensure that its UCC filings are up to date and shall remain in effect for the duration of the loan.

Section 7: Documentation Custodian, Loan Servicing, & Loan Monitoring

(A) Document Custodian Generally:

The HUD Section 108 program requires that the City appoint a financial institution or title company to act as document custodian for all documents related to individual loans originated under the HUD Section 108 loan program. The City may in its discretion select one or more institutions to perform this task. The City and applicant Borrower may choose an institution that is mutually agreeable to serve as custodian of documents as well as to serve as a point of remittance for the Borrower for all payments made under the loan program.

(B) Credit Files:

The City shall maintain in its records all credit related information related to Borrower throughout the duration of any loan made under this program.

(C) Loan Documentation & Servicing:

In order to ensure that Borrower payments are made when due and to properly service and enforce loan covenants, the City shall maintain properly drafted and executed documents for every loan to be made. As mentioned above, all security agreements and UCC forms must be keep active and properly recorded with the Secretary of State. The City will ensure that timely repayment of loans be made by creating an invoice system that will require invoices to be made several weeks in advance of due dates.

Section 8: Loan Document Checklist:

Outlined below are loan documents and other items that the City Staff will maintain during the loan closing process. Each loan will have a file with this Checklist in front.

Name of Borrower:_______________________________________
Address:____

General Requirements:

- ☐ Executed Loan Agreement
  - ☐ Job Creation Covenant
  - ☐ Description of Eligible Costs
  - ☐ Disbursement Procedures Outline
  - ☐ Document Custodian Bank Agreement
- ☐ Executed Promissory Note & Amortization Schedule
- ☐ Executed Security Agreement and UCC Filing Statements
  - ☐ Evidence of Security Agreement filings (receipts from Sec. of State)
  - ☐ Appraisal Report (if security is real property)
  - ☐ Legal Description of property (if security is real property)
  - ☐ Title Report/insurance (if security is real property)
- ☐ Unconditional Personal Guarantee
- ☐ Corporate Guarantee
- ☐ Stand-By Agreement
- ☐ Insurance
  - ☐ Hazard Insurance on collateral with City named as loss payee
  - ☐ Key person life insurance (optional)
  - ☐ Business interruption insurance (optional)
  - ☐ Builder's risk insurance (optional)
- ☐ Current Organizational Document for Borrower:
  - ☐ Secretary of State Cert. of Good Standing
  - ☐ Corporate Organization Documents (Articles of Organization, Incorporation, etc.), By-laws, Operating Agreements;
  - ☐ Copies of Business Leases with Landlord (if applicable)
  - ☐ Assignment of leases, rents and profits
  - ☐ Copies of any management agreements
- ☐ Construction Contract (if applicable)
- ☐ Copies of Invoices on all M&E and equipment purchases (if applicable)
- ☐ Copy of Executed Sales Contract (if loan involves purchase of land)

Section 9: Definitions:

City – as used in this Document shall mean the City of Brockton acting by and through the Brockton Redevelopment Authority.

Fixed Asset- permanent business properties such as land, buildings, machinery and equipment.

Gap Financing- The portion of funds supplied by the City through the Downtown Restaurant Infrastructure Fund that will allow a business to expand, start-up, or otherwise remain in business, that absent this assistance would not take place.

Job – shall mean a permanent, full-time equivalent employment measured according to a period not less than 365 days, consistent with HUD guidance concerning job creation under the CDBG program.

Job Retention- shall me a job that would be lost or otherwise relocated outside of the municipal jurisdiction of the City of Brockton but for the financial assistance provided under this program. The business applying for the funds must prove to the satisfaction of the Loan Review Committee that the provision of financial assistance is necessary to achieve the job retention goal.

Job Creation – shall mean a job that is a budgeted position to be filled within six months that was not in existence prior to the provision of financial assistance. The job must be tangible, and the applicant must commit and certify that this job will be filled within the delineated time period following the provision of the financial assistance from the City of Brockton.

Loan Review Committee- shall refer to the five (5) person body established by the Brockton Redevelopment Authority for the purposes of evaluating prospective loans under the Downtown Restaurant Infrastructure Fund program. The Loan Review Committee shall be comprised of five (5) members, three (3) members of which will be City employees with expertise in financial analysis and/or business credit, appointed by the Brockton Redevelopment Authority. The two (2) non-municipal members of the Loan Review Committee should be individuals with extensive experience in financial underwriting.

Low- and Moderate-Income – shall refer to the individual income levels as published by HUD for the CDBG and HOME programs. The levels are generally calculated as 80% of an area's median income adjusted for family size. The most recent data for such determinations can be found on the HUD website at: www.hud.gov .

Market Analysis – shall refer to the objective process by which the need, market potential and expected return on investment is determined for a particular product and/or service.

Working Capital – shall refer to the funds available and necessary for normal business operations. A Working Capital Type Loan is a loan whose purpose is to finance everyday operations of a company. Working capital loans are a means for businesses to generate capital and to start being focused on business growth.