
CHALLENGE LOANS

1. PURPOSE

To provide loan policies and procedures that are uniform and for quality control to ensure good, consistent service.

2. SCOPE

The Wyoming Business Council Board of Directors and any staff that has oversight of the Challenge loan portfolio or loan administration responsibilities. Please refer to the Wyoming Partnership Challenge Loan Program Rules and Regulations for detailed requirements and procedures.

3. DEFINITIONS

"Borrower" means the community development organization or a state development organization, which applies for, commits to, and is responsible for repayment of funds provided under this program;

"Business" means any existing enterprise which employs people within the state, provides services within the state, uses resources within the state or otherwise adds economic value to goods, services or resources within the state, and includes farm and ranch operations;

"Cash or cash equivalent" means liquid assets including savings, checking and money market accounts, certificates of deposit, stocks, bonds or cash value life insurance or other similar assets. Equity in real estate holdings and other fixed assets is not to be considered liquid assets;

"Commercial Lender" means commercial institutions that loan money, including banks, credit unions, mutual savings banks, savings and loan associations, stock savings banks, or trust companies.

"Community development organization" means a group of private citizens organized as a business entity authorized to do business in this state for the purpose of providing financing for new, existing, or expanding businesses and other economic or community development purposes in Wyoming, and which may take equity positions and shall take security positions in its borrowers' businesses and appropriate personal guarantees from the owners thereof;

"Economic Disaster Loan(s)" means loans made to eligible businesses in an economic disaster area as defined by W.S. 9-15-301(a)(v), where such loans are funded by the Challenge Loan Program;

"Servicing agent" means the qualified entity contracted by the WBC to service the loans in the portfolio and to provide administrative services for the program;

"State development organization" means a corporation organized under W.S. 17-11-101 through 17-11-120 with the authority to provide financing for new, existing or expanding businesses, and to fulfill other economic or community development purposes throughout the state of Wyoming, and which may take equity positions and shall take security positions in its borrowers' businesses and appropriate personal guarantees from the owners thereof; and

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“Main street loan participation” means a provision of financing by the WBC in which the WBC participates with a Commercial Lender that has made a loan to a business for building improvements to maintain the structure’s historical character.

“Natural gas fueling infrastructure loan” means a loan issued by the WBC for the costs of the engineering, design, real property, equipment and labor necessary to install a functioning natural gas filling station to fuel motor vehicles, which operate on natural gas as a transportation fuel.

4. OVERVIEW

Loan standards and procedures that are uniform throughout the WBC are necessary for quality control to ensure good, consistent service to the WBC's borrowers, and fiduciary responsibility to the State of Wyoming and the Federal Government. Uniform standards will allow the WBC to be familiar with the normal requirements for each type of loan in its portfolio.

4.1 Responsibilities

The responsibility for the WBC's lending activities shall rest with the Board.

The Board will establish a committee from within to work with and modify loan policy standards. The loan committee will also function at the Board’s direction and among other things, present new loans for approval, review and approve loan renewals, extensions, amendments, reserves, write-offs, or other duties the Board considers necessary and delegates.

4.2 General Policy

The Board, in making loans and providing direction to other WBC personnel and servicing agents engaged in the preparation, administration and safekeeping of loan documents shall be guided by the following Loan Policy as adopted by the Board.

The basic loan policy of the WBC will be to provide financing to business entities in the State of Wyoming in an effort to promote economic development within the State and to service the loan portfolio in a responsible manner. Financing provided by the WBC is intended to be an alternative and/or compliment to existing commercial financing sources that are available, not as the primary lending source. All loans should be made in anticipation of transitioning the borrowing needs from the WBC to commercial sources.

The provision of finance at below-market interest rates, when viewed in terms of a risk-adjusted return basis, should be done only when necessary to assist/incite businesses expanding or relocating to Wyoming. The WBC believes that companies that have been financed by the WBC or other state sources should ultimately be financed by the private sector. Therefore, when the WBC is providing a loan, the loan terms should be structured to build in interest rate increases over time, in order to make the WBC/State loans as expensive as those provided by commercial lenders, and thereby encourage refinancing.

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The Board realizes that lending of money by the WBC necessarily includes some business risk and some losses are to be expected. It is the policy of the Board to maintain a reserve for future loan losses. Loans, with the approval of the Board, may be charged off only after such loans have received maximum collection effort.

5. LOAN POLICY

The basic loan policy of the WBC will be to service the borrowing needs of entities that enhance the economic development of the State of Wyoming on a sound and prudent basis that is beneficial to the people of Wyoming.

The Board, in discharging its duty, will ensure that loans in the WBC's portfolio are made on a sound and collectable basis promoting economic development within statutory authorization.

5.1 Types of Loans

The types of loans and financing the WBC will provide to entities in promoting economic development are as follows:

(1) Commercial Loans

- a. Loans secured by a security interest in marketable equipment are to be amortized over a period not to exceed 120 months. The loan should not exceed 85% of value.
- b. Working capital loans secured by inventory and/or accounts receivable should be made to a borrower whose financial condition and income clearly indicate an ability to repay without resorting to liquidation of inventory and/or the accounts receivable securing the loan. The terms of these loans should not exceed one year and an aging schedule and inventory listing should be updated at least quarterly. The loan should not exceed 50% of the value of the eligible inventory and 60% of the value of the eligible accounts receivable. Eligible accounts receivable include only those accounts that are not more than 60 days past due. Eligible inventory would exclude inventory that is not marketable or obsolete.

(2) Real Estate Loans

- a. Permanent real estate loans secured preferably by first mortgages on improved business or commercial properties. Real estate loans including any prior liens shall not exceed 85% of appraised value and loan maturity shall not exceed 240 months.
- b. Main Street Loan Participation: A provision of financing by the WBC in which the WBC participates with a Commercial Lender that has made a loan to a business, preferably located in the downtown area of a municipality, for building improvements to maintain the structure's historical character.

(3) Economic Disaster Loans

Economic disaster loans will be granted only after an economic disaster has been declared, as defined by law and adopted rules.

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- a. The WBC can only approve loans to applicants with a reasonable ability to repay the loan and other obligations from earnings. The terms of each loan are established in accordance with each borrower's ability to repay but shall not exceed 120 months.
- b. As required by law, the interest rate for each loan is based on the WBC's determination of whether each applicant has the ability to repay. Substantial economic injury is the inability of a business to meet its obligations as they mature and to pay its ordinary and necessary operating expenses.

(4) Natural gas fueling infrastructure loans

Natural gas fueling infrastructure loans are direct loans from the challenge loan program for natural gas fueling infrastructure.

- a. Funds must be used for the costs of the engineering, design, real property, equipment and labor necessary to install a functioning natural gas fueling station.
- b. Payment terms consist of no interest or principal payments due for the first two (2) years of the term loan. All deferred interest during the first two (2) years of the term loan shall accrue to the principal balance.
- c. Loans are to be amortized over a period not to exceed 240 months. Loans should not exceed 75% of the total costs of land, building and equipment or one million dollars (\$1,000,000), whichever is less.

(5) Future Investment or Loan Programs

Modifications will be made to the policy in this chapter as necessary to reflect changes made to existing state statute.

5.2 Loans Not Considered Desirable

The following loans are not considered desirable for the purpose of the WBC. Such loans will ordinarily be declined unless specifically approved by the Board for reasons that justify an exception to this policy.

- (1) Loans that do not promote economic development within the State of Wyoming.
- (2) Real estate mortgage loans secured by proceeds of the settlement of an estate, unless these loans are fully collateralized or guaranteed by the estate and approved by the Council's attorney.
- (3) Loans secured by stock in a closed corporation which has no ready market.
- (4) Loans secured by restricted or lettered stock.
- (5) Capital loans to a business enterprise in which the loan cannot be repaid within a reasonable period except by borrowing elsewhere or by liquidating the business.
- (6) Unsecured loans.

5.3 Appraisal Program for Loans Involving Real Estate

Appraisals shall be performed by a qualified, independent fee paid appraiser

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selected by the WBC or lead lender who is competent and knowledgeable of the relevant markets. The WBC does not favor appraisers from one or more councils or exclude individuals based on their lack of such membership. The appraisal policy will be based on compliance with Part 323 of Federal Deposit Insurance Corporation Rules and Regulations on transactions with a value of \$250,000 or more. This regulation identifies which transactions by financial institutions require an appraisal by a certified or licensed appraiser.

The appraisal should conform to the Uniform Standards of Professional Appraisal Practice (USAP) adopted by the appraisal standards Board of the Appraisal Foundation. For transactions that are otherwise exempt from appraisal requirements, an appropriate evaluation of the real property will be performed. However, prudent lending standards still require that such loans and other real estate related transactions be supported by adequately prepared estimations of collateral value. An independent appraisal is one in which the appraiser is not involved in the loan.

The appraisal performed by independent staff must reflect a value and an analysis as to how the value is determined. Any deviation from this policy will also be based on compliance with Part 323 of Federal Deposit Insurance Corporation Rules and Regulations. If a real estate loan is renewed, a new appraisal is not required if:

- (1) The borrower has performed satisfactorily according to the original terms.
- (2) No additional money has been advanced other than as previously agreed.
- (3) The credit standing of the borrower has not deteriorated.
- (4) There has been no significant deterioration in market conditions or physical aspects of the property that would threaten the collateral protection.

Part 323.3(b) of the FDIC Rules and Regulations requires appropriate evaluations for real estate-related transactions that do not require the services of a state certified or licensed appraiser.

In the event an appraisal is not required for a transaction involving an existing extension of credit an evaluation may be obtained, provided that:

- (1) There has been no obvious and material change in market conditions of physical aspects of the property that threatens the adequacy of the institution's real estate collateral protection after the transaction, even with the advancement of new monies; or
- (2) There is no advancement of new monies, other than funds necessary to cover reasonable closing costs.

5.4 Environmental Risk

Loans to be secured by real estate must be carefully examined for possible environmental risk through an environmental review that will be completed prior to loan processing.

The WBC should focus on hazardous construction materials (e.g. lead paint, asbestos), hazardous waste storage sites, leaking drums, retention ponds,

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discolored vegetation, underground storage tanks, and adjacent properties. Any evidence of environmental contamination will require a more detailed assessment; the results of which may dictate the borrower remediate the hazardous waste before closing the loan. In addition, during the due diligence process prior to making the loan, the WBC's Business Finance Program Manager should determine if the borrower shall execute warranties and indemnifications at the closing as to the property's environmental condition and proposed use.

5.5 Repayment Terms

All loans should have a realistic repayment plan. The maturity of the loan should be related to the anticipated source of repayment, cash flow of the borrower, purpose of the loan, the useful life of the collateral and be consistent with State Statutes.

Collateral does not repay loans; cash flow repays loans. The collateral package provided as security should reflect the source of repayment. At all times, the collateral should be sufficient to adequately protect the commercial lender from a decline in market value. Substantial collateral does not alone justify an extension of credit.

Extensions may be granted with the approval of the Board.

A fee will normally be assessed with any extensions approved.

5.6 Guaranty of Loans

It is the policy of the WBC that all loans to closely held companies will be guaranteed by the principals of the company. Where this requirement is waived, it must be substantiated by the financial strength of the company and documented in the credit file. Any deviation from this policy must have the prior approval of the Board.

5.7 Loan Authority

All loans require approval of the Board. All loan requests are to be submitted to the WBC for recommendation and completeness. The loan request is then forwarded to the business development subcommittee, and ultimately to the Board for consideration. All presentations to the Board will include at a minimum the following information:

- (1) Borrower's name
- (2) Business/project description and purpose of the loan request
- (3) Amount of loan
- (4) Term of loan
- (5) Proposed interest rate
- (6) Economic development benefits to the State of Wyoming
- (7) Total repayment program
- (8) Financial information and analysis demonstrating an ability to repay the loan
- (9) Risks and mitigants
- (10) Proposed guaranty(s)
- (11) Proposed collateral

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- (12) Value of collateral
- (13) Terms and conditions of the proposed loan agreement, including covenants

6. UNDERWRITING GUIDELINES

The primary goal of the lending activities of the WBC should be to stimulate economic growth and development, and to transition the borrowers funding needs to commercial sources as individual business results warrant. All loans should have appropriate terms to facilitate the transition of the loan(s) to commercial sources.

The WBC will provide financing to credit worthy businesses but not as the primary lending source. The intent to participate with private-sector lenders is that the lead lender performs their own, independent review (a "second set of eyes") of the credit worthiness of the borrower, thereby minimizing the public sector exposure.

Loan terms should be structured to build in interest rate increases over time, in order to make the WBC/State loans as expensive as those provided by commercial lenders, thereby encouraging refinancing.

The WBC may impose loan terms, conditions and covenants in order to monitor loan performance and economic development. Examples of those terms, conditions, and covenants, which would be established on a loan-by-loan basis include:

- (1) No dividends or other shareholder distributions, except for loans with S-Corporations and partnerships whereby income taxes are assessed at the shareholder level. Those distributions will require prior approval by the WBC.
- (2) Limitations on shareholder salaries and increases in shareholder salaries.
- (3) Restrictions on additional indebtedness, salary increases, capital expenditures.
- (4) Restrictions for lease payments for the use of property and equipment owned by affiliated entities.
- (5) Pre-established ratios and other specifically identified measurement requirements.
- (6) Periodic reports, including financial statements and other reports deemed necessary to monitor the operations of the business and the economic development impacts within the State of Wyoming.

Interest rates and loan terms should be realistic based on the business operations, yet include escalating interest rates, terms, conditions, and covenants to promote the transition of the borrower to existing commercial funding sources.

7. LOAN ADMINISTRATION

The WBC shall prepare a credit application/memorandum to the credit file for each type of loan. The credit application/memorandum will be in writing and will cover the following points:

- (1) The credit worthiness of the borrower
- (2) The purpose of the loan
- (3) The economic development benefits for making the loan
- (4) Financial statement analysis to show an adequate source of repayment

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- (5) Collateral/guarantor analysis to demonstrate adequate backup sources of repayment
- (6) Personal guarantees by corporate officers/shareholders if a closed corporation
- (7) An analysis of whether a business plan or pro-forma financial statements are required
- (8) Other information used to come to a decision on making the loan

Maximum loan to value shall not exceed 85%, unless otherwise specified, however a borrower may desire to finance 100% of the project cost and may provide additional collateral in lieu of cash down payment.

A credit file shall be established and maintained for each borrower, which shall include in all cases the borrower's current financial statement, tax returns and the credit application/ memorandum. Loan agreements should clearly identify the borrower's responsibility for providing future financial information including required information (e.g. Audited financial statements, internal financial statements, tax returns, compliance with loan covenants, required UCC updates, etc) and when such information is due to the WBC and/or servicing agent. The information needs and due dates will be compiled into a database that will be used to establish a tickler system to maintain compliance with this policy. The credit file will include copies of all documents and correspondence pertinent to each loan.

Loan administration may be delegated to a servicing agent approved by the Board. The contract with the servicing agent will specify those duties and responsibilities to be performed, including reporting to the WBC and/or the Board on a frequent basis.

Minimum documentation for real estate loans shall include the promissory note, environmental check, a written recorded copy of the mortgage, Title Opinion or Title Insurance, a copy of the appraisal of the property, and an insurance certificate or binder insuring the property against damage and showing the WBC / or lead lender as loss payee.

Minimum documentation for loans secured by marketable equipment shall consist of the promissory note, a security agreement that can be supported by a financing statement. At least one of these documents must be filed with the appropriate authority. Documentation on loans made on the titled equipment shall include, in addition to the security agreement, recorded copies of the title showing the WBC / or lead lender as the secured party and an insurance certificate or binder insuring the property against damage and showing the WBC / or lead lender as loss payee.

All personnel shall take the utmost care in the security and safekeeping of loan documents. All promissory notes shall be kept in a secure fireproof location. The WBC or its designee shall conduct loan review documentation on a continuing basis for all loans. Notices of due dates for each loan shall be supplied to the Business Finance Program Manager ten days before maturity.

Interest due on loans is to be collected from borrowers according to the terms and conditions of the loan agreement and note. The WBC should not add interest due to the unpaid principal balance on any loan on which interest is due unless approved by the Board and supported by additional tangible collateral, which adequately and completely secures the loan or uncollected interest booked to income.

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8. LOAN REVIEW

Successful loan review systems have specified time frames for reviews, accountability through required reporting to the proper level of the organization and a consistently applied system. Loan reviews should be performed by an individual independent of the normal administration of loans so that the review provides a new perspective on the reviewed loan.

The portfolio is currently very small and each loan is reviewed for credit quality and documentation requirements annually either by the Department of Audit, Division of Banking or the Independent Auditors Financial Report. These external audits will be the loan review process until the portfolio grows and becomes more seasoned requiring a detailed internal review procedure.

9. RESERVE FOR LOAN LOSS POLICY

The WBC will implement the policies and procedures as a means of analyzing the adequacy of the loan loss allowance on an ongoing basis. The purpose of the analysis will be to identify the risks in the loan portfolio and assure the allowance is adequate should those risks become future losses. Items that should be considered when identifying such risks are listed in Appendix A to this chapter.

The adequacy of the allowance will be made at the end of each quarter and reports, as specified in this policy, of the analysis will be presented to the Board. The Board will determine if the reserve is adequate.

The reserve will be arrived at per the following:

- (1) All loans that are delinquent (over 30 days past due) will be reviewed. A specific reserve will be allocated for each of these loans if the review warrants.
- (2) There will be an additional unallocated reserve of one-half of one percent of the total portfolio balance.
- (3) There will be a 10% reserve for Economic Disaster loans.

10. LOAN COLLECTIONS

10.1 Collections

The WBC has reasonably conservative loan polices designed to preclude delinquencies and losses in the loan portfolio. If polices are followed, the WBC should not experience an undue amount of collection problems. Successful collections and workouts depend on early identification of credit weaknesses so the relationship between loan collections and loan monitoring cannot be emphasized enough.

A 10-day notice in advance of maturity is mailed. Late notices are to be sent on the 10th day a note becomes delinquent. Contacts and collection efforts should be started on the 10th delinquent day. From that point forward, all remarks pertaining to the workout of the delinquent account should be dated with the day, month, and year the contact is made. All loans 30 days or more past due are required to be reported to the Board.

Late charges are not only a deterrent to late payment by the borrower but also compensate the WBC for the extra cost of collection and loss of use of the payment

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amount. It is the WBC's policy to collect all late charges and great selectivity will be exercised in making any exceptions. In addition, interest will be collected to the actual date of payment for loans paid after maturity.

Once a decision has been made to call the loan, the following steps will be taken:

- (1) The WBC will consult with its attorney in all matters.
- (2) It is preferable that the note be past due when the note is called. If, while working a problem loan the note must be renewed, it should either be renewed as a demand note or it should contain an enforceable clause.
- (3) Once a decision has been made for demand of a note, a letter is sent which spells out the reasons the WBC is making demand. The WBC's policy is not to use demand letters as idle threats. The WBC does not send demand letters until it is ready to call the loan.
- (4) The collateral securing the loan must be protected. The WBC may take physical possession of the collateral early in the process or the WBC may take a physical inventory.
- (5) It is important that the WBC does not lose its guarantees by oversight during the liquidation process.

10.2 Renewals and Extensions

All requests to renew, defer, or extend existing loans shall be considered under the same process as the underwriting standards and documentation for the initial provision of credit. The loan should not be renewed or extended if alternative private sources of funding are available. The loan(s) should not compete with commercial funding sources.

The Board or its designee shall review all renewals and these shall be treated as any other loan with respect to the Board's authority and approval. No extensions or renewals will be granted without the approval of the Chief Executive Officer. It is customary that if such requests are granted, that amendment fees are appropriate, as well as a potential change in interest rates and other terms. Potential problems will be immediately and appropriately dealt with. Renewals, deferments, and extensions shall not be used to defer a potential problem or loss to a later date.

It is important for the WBC to maintain its position in regards to the collateral; therefore, renewal or extension of a loan may be necessary to accomplish this objective. On any extension or renewal, a complete comment shall be placed in the credit file as to the nature of the extension or renewal, new interest rate, maturity date, etc. Also, updated remarks will be noted. In most circumstances, no loans will be extended or renewed unless interest has been paid to the date of renewal or extension.

10.3 Non-Accrual of Interest

The WBC will not accrue interest and report income in the WBC's financial statements when:

- (1) Any loan which is maintained on a cash basis because of the deterioration in the financial position of the borrower.
- (2) Any loan for which payment in full of interest or principal is not expected.

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- (3) Any loan upon which principal or interest has been in default for a period of 90 days or more unless it is both well secured and in the process of collection.

From the perspective of the borrower's liability to the WBC, the loan will continue to accrue interest in accordance with the terms of the loan agreement.

A non-accrual loan may be restored to an accrual status when none of its principal and interest is due and unpaid or when it otherwise becomes well secured and in the process of collection.

11. LOAN CHARGE-OFF PROCEDURES

It is the WBC's policy to charge-off those loans whose collectability is sufficiently questionable that the WBC can no longer justify showing the loan as an asset in its financial statements. These loans are charged-off by crediting the appropriate loan category and debiting the reserves for loan accounts. Charged-off loans must be approved by the Board prior to charging-off.

Collection efforts will continue on all charge-off loans unless the balance is determined uncollectable due to bankruptcy, complete liquidation and settlement agreement, death or any other occurrence, which will render the balance uncollectable.

A report will be presented at each Board meeting updating collection efforts.

12. REPORTING REQUIREMENTS

Reporting requirements to the Board or its designee with respect to the loan portfolio will include the following:

- (1) Listing of loans 30 days or more past due provided at each Board meeting.
- (2) Computation of allowance for loan losses provided at each Board meeting.
- (3) Report of examination by the Department of Audit, Division of Banking will be presented at the first Board meeting following the receipt of the report.
- (4) Report as required by W.S. 9-12-306(b) to the Board prior to July of each year.
- (5) Report on charge-off collection efforts at each Board meeting.