



Government of the District of Columbia
Department of Insurance, Securities and Banking



STATE SMALL BUSINESS CREDIT INITIATIVE

DISTRICT OF COLUMBIA COLLATERAL SUPPORT PROGRAM
(“DCCSP”)

Participating Lender Guide

MAY 2013



DISTRICT OF COLUMBIA COLLATERAL SUPPORT PROGRAM

On September 27, 2010, President Obama signed into law the Small Business Jobs Act of 2010 (the “Act”) to help increase credit availability for small businesses. The Act created the State Small Business Credit Initiative (“SSBCI”) at the U.S. Department of the Treasury (“Treasury”), which allowed the District of Columbia Department of Insurance Securities and Banking (the “DISB”) to receive an allocation of \$13,168,350 to fund the D.C. Collateral Support Program (the “DCCSP” or the “Program”). The DCCSP establishes pledged cash collateral accounts with Participating Lending Institutions to enhance loan collateral for qualified small business borrowers that would not otherwise be able to obtain financing on acceptable terms and conditions. Cash collateral deposits are established on an individual loan basis and are available to cover loan losses in the event of default by the borrower. During the term of the loan, the deposits are gradually returned to the DCCSP on an annual basis for recycling to other qualified small business borrowers.

A Participating Lender must be a state or federally chartered bank, insured credit union, or community development financial institution that has signed a Participation Agreement with the DISB. Participating Lenders apply to the DISB for collateral support deposits on behalf of qualified small business borrowers. Participating Lenders are responsible for their own credit underwriting decisions, as well as the origination and servicing of loans. The DISB’s responsibility is to ensure compliance with the DCCSP requirements, establish and manage collateral support accounts, and to report to the U.S. Department of Treasury. The DISB will also assist in promoting and marketing the DCCSP and interested small businesses will be referred to Participating Lenders.

The following is intended as guidance to assist Participating Lenders in understanding the federal and District’s compliance requirements of the SSBCI and the DCCSP. The numbered headings below correspond with the numbered headings in the Loan Enrollment Form and Eligibility Questionnaire, beginning on page 3.



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1. Eligible Lender

- a. **Capital at Risk:** For any loan enrolled in the Program, the Participating Lender must have a meaningful amount of its own capital at risk, consistent with OMB Circular No. A-129, “Policies for Federal Credit Programs and Non-Tax Receivables.” Accordingly, a Participating Lender must demonstrate that it will bear at least twenty percent (20%) of the loss from a default on an enrolled loan. Treasury will consider any enhancement that Congress extends to the SBA Section 7(a) Loan Guarantee Program in which financial institution lenders may bear less than twenty percent (20%) of the risk as analogously applicable to the Program. Under such circumstances, the Program may allow financial institution lenders to bear the same amount of risk as similarly situated financial institution lenders under the SBA Section 7(a) Loan Guarantee Program.
- b. **Privacy and Customer Identification:** Each Participating Lenders must certify its compliance with the requirements of 31 C.F.R. § 103.21, which implements section 3261 of the Patriot Act and relates to procedures for anti-money laundering programs. Under the regulation, banks, savings associations, credit union, and certain non-federally regulated banks are required to implement a written Customer Identification Program. Moreover, to the extent a Participating Lender is asked to disclose to the DISB or Treasury Inspector General the books and records related to the enrolled Borrower, the Lender must comply with the requirements of the Rights to Financial Privacy Act (12 U.S.C. § 3401 et seq.). The Right to Financial Privacy Act is a federal law that gives customers of financial institutions the right to some level of privacy from government searches. Certification will be made upon execution of the Cash Collateral Deposit Agreement.
- c. **Sex Offense:** Each Participating Lenders must certify that none of its principals have been convicted of a sex offense against a minor, as such terms are defined in section 111 of the Sex Offender Registration and Notification Act (42 U.S.C. § 16911). A principal is defined as a proprietor, partner, director, each of the five most highly compensated executives, officers, or employees of the Participating Lender, or each direct or indirect holder of twenty percent (20%) or more of the ownership stock or stock equivalent of the Participating Lender. Certification will be made upon execution of the Cash Collateral Deposit Agreement.



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2. Eligible Borrower

- a. **Number of Employees:** The Program targets an average Borrower size of five hundred (500) employees, as defined in 13 CFR § 121.106 or less and cannot extend collateral support to Borrowers with more than seven hundred fifty (750) employees. The Borrower, including its affiliates and subsidiaries, must have seven hundred fifty (750) or fewer employees at the time the loan is enrolled in the Program.
- b. **Certified Business Enterprise (CBE):** The Borrower must be eligible for CBE certification, a designation granted by the D.C. Department of Small and Local Business Development. The Borrower must submit its application for CBE certification before the Participating Lender can make its Reservation of Funds request. The Borrower must obtain CBE certification before loan closing date.
- c. **Total Amount of Enrolled Loans:** The maximum aggregate outstanding loan amount(s) that may be enrolled for any single Borrower or any common enterprise in which the Borrower has an ownership interest is five million dollars (\$5,000,000).
- d. **Collateral Support Needs:** The maximum amount that the DISB may pay into a Cash Collateral Account on behalf of a single Borrower is fifty percent (50%) of the loan amount or no more than one million dollars (\$1,000,000).
- e. **Personal Guaranties:** Personal guarantees are required from any individual holding twenty percent (20%) or more ownership interest in the Borrowing Entity.
- f. **Sex Offense:** Each Borrower must certify that none of its principals have been convicted of a sex offense against a minor, as such terms are defined in section 111 of the Sex Offender Registration and Notification Act (42 U.S.C. § 16911). A principal is defined as a proprietor, partner, director, each of the five most highly compensated executives, officers, or employees of the Borrowing Entity, or each direct or indirect holder of twenty percent (20%) or more of the ownership stock or stock equivalent of the Borrowing Entity. Certification will be made upon execution of the Cash Collateral Deposit Agreement.



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3. Prohibited Borrower Activity

- a. **Speculative Activities:** The Borrowing Entity must not be engaged in speculative activities that derive profit from fluctuations in price, such as wildcatting for oil and dealing in commodities futures, unless those activities are incidental to the regular activities of the business and part of a legitimate risk management strategy to guard against price fluctuations related to the regular activities of the business.
- b. **Lending Activities:** The Borrowing Entity must not earn more than half of its annual net revenue from lending activities, unless the Borrowing Entity is a non-bank or non-bank holding company that is certified as a Community Development Financial Institution.
- c. **Pyramid Sales:** The Borrowing Entity must not be engaged in pyramid sales, where a participant's primary incentive is based on the sales made by an ever-increasing number of participants.
- d. **Illegal Activities:** The Borrowing Entity must not be engaged in activities that are prohibited by federal law or laws of the District of Columbia. Included in these activities is the production, servicing, or distribution of otherwise legal products that are to be used in connection with an illegal activity, such as selling drug paraphernalia or operating a motel that knowingly permits illegal prostitution.
- e. **Gambling:** The Borrowing Entity must not be engaged in gambling enterprises, unless the business earns less than thirty-three percent (33%) of its annual net revenue from lottery sales.

4. Conflicts of Interest

- a. **Borrower-Lender:** The Borrower must not be an executive officer, director, or principal shareholder of the Participating Lender providing the credit facility.
- b. **Borrower's Immediate Family-Lender:** The Borrower must not be a member of the immediate family of an executive officer, director, or principal shareholder of the Participating Lender providing the credit facility.



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- c. **Borrower's Related Interest-Lender:** The Borrower must not be a related interest of such an executive officer, director, or principal shareholder, or member of the immediate family of the Participating Lender providing the credit facility.

5. Impermissible Use of Funds

- a. **Passive Investments:** The Borrower must not use loan proceeds to acquire or hold passive investments, unless Borrower meets one of the four following conditions:
- i. If loan proceeds are used to acquire, renovate, or reconstruct an existing building, Borrowing Entity must occupy no less than fifty-one percent (51%) of total rentable space* within twelve (12) months of the acquisition. The Borrower may lease up to forty-nine percent (49%) of the rentable space to third parties. Under no circumstances can loan proceeds be used to improve or renovate any of the rentable space that is leased to a third party. See example below.**
 - ii. If loan proceeds are used to construct a new building, Borrowing Entity must occupy no less than sixty percent (60%) of the total rentable space following construction. The Borrower may lease up to forty percent (40%) of the rentable space to third parties. Under no circumstances can loan proceeds be used to improve or renovate any of the rentable space that is leased to a third party.
 - iii. If the Borrower is a holding company that will use the loan proceeds to acquire, renovate, or reconstruct an existing building, the Borrower must lease no less than fifty-one percent (51%) of the total rentable space within twelve (12) months of the acquisition to an operating company that is an eligible business (i.e. a business not engaged in any of the prohibited activities listed in Section 3 above). The Borrowing Entity or the Operating Company may lease up to forty-nine percent (49%) of the rentable space to an unaffiliated company. Under no circumstances can loan proceeds be used to improve or renovate any of the rentable space that is leased to an unaffiliated company. In addition to the occupancy requirements, all of the following conditions must be met:
 1. The Operating Company is a guarantor or co-borrower on the Enrolled Loan;



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2. Both the Borrowing Entity and the Operating Company must execute the Certifications, including Sex Offender Certifications, and Assurances in the Cash Collateral Deposit Agreement;
 3. Each natural person holding an ownership interest constituting at least twenty percent (20%) of either the Borrowing Entity or the Operating Company must provide a personal guaranty for the Enrolled Loan; and
 4. The Borrowing Entity and the Operating Company have a written lease agreement with a term at least equal to the term of the Enrolled Loan.
- iv. If the Borrower is a holding company that will use the loan proceeds to construct a new building, the Borrower must lease no less than sixty percent (60%) of the total rentable space following construction to an operating company. The Borrowing Entity or the Operating Company may lease up to forty percent (40%) of the rentable space to an unaffiliated company. Under no circumstances can loan proceeds be used to improve or renovate any of the rentable space that is leased to an unaffiliated company. In addition to the occupancy requirements, all of the following conditions must be met:
1. The Operating Company is a guarantor or co-borrower on the Enrolled Loan;
 2. Both the Borrowing Entity and the Operating Company must execute the Certifications, including Sex Offender Certifications, and Assurances in the Cash Collateral Deposit Agreement;
 3. Each natural person holding an ownership interest constituting at least twenty percent (20%) of either the Borrowing Entity or the Operating Company must provide a personal guaranty for the Enrolled Loan; and
 4. The Borrowing Entity and the Operating Company have a written lease agreement with a term at least equal to the term of the Enrolled Loan

**Rentable space* is defined as all of the square footage used for business operations including common areas but excluding vertical penetrations (i.e. stairways, elevators, mechanical areas designated to transfer people or services vertically between floors), common areas (i.e. lobbies, passageways, vestibules, and bathrooms), and all outside areas.



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** For example, Smith Bakery may use the proceeds of an SSBCI-supported loan to purchase an existing building with 4,000 square feet of rentable property that is currently leased to three businesses if at least 2,040 (51%) square feet will be occupied by the bakery itself within 12 months of acquiring the building.

The Borrower must provide substantiating documents to ensure the occupancy requirements are met. Such documents may include lease agreements, blueprints, or similar documentation.

- b. **Evangelizing, Proselytizing and Lobbying:** The Enrolled Loan must not be used for evangelism, proselytizing, or lobbying activities.
- c. **Repayment of delinquent income taxes:** The Enrolled Loan must not be used to repay delinquent federal or District of Columbia income taxes unless the Borrower has a payment plan in place with the relevant taxing authority.
- d. **Repayment of taxes held in trust or escrow:** The Enrolled Loan must not be used to repay taxes held in trust or escrow, for example, payroll or sales taxes.
- e. **Reimbursement of funds owed to owners:** The Enrolled Loan must not be used to reimburse funds owed to any owners of the Borrowing Entity. This includes any equity injection or injection of capital for business continuance.
- f. **Purchase of ownership interest of an owner:** The Enrolled Loan must not be used to purchase any portion of the ownership interest of any owner of a business. For example, an acquisition of stock or other goodwill is prohibited; however, an asset purchase from an existing business is permitted.
- g. **Unguaranteed portion of an SBA loan:** The Participating Lender must not enroll in the DCCSP the unguaranteed portion of an SBA loan.
- h. **Use of Proceeds outside of D.C.:** The Borrower must demonstrate and certify that the loan proceeds will be used within the District of Columbia or that the loan will fund the salaries of District residents working on Borrower's projects outside of the geographic territories of the District of Columbia. Certification will be made upon execution of the Cash Collateral Deposit Agreement. In addition, the Borrower must cooperate with the Participating Lender and the DISB to provide the estimated number of jobs created and retained as a result of the Enrolled Loan.



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6. Refinancing

- a. **Same Lender:** Participating Lenders may use DCCSP funds to support a new extension of credit or refinance an existing debt held by the same Participating Lender if the new extension of credit or refinancing repays the amount due on a matured loan or line of credit and when all of the following conditions are met:
 - i. The new loan or line of credit includes the advance of new monies to the Borrower, and the new monies cannot include closing costs;
 - ii. The new credit supported with DCCSP funding is based on new underwriting of the Borrower's ability to repay and a new approval by the Participating Lender;
 - iii. The proceeds from the new credit may only be used to satisfy the outstanding balance of a loan or line of credit that has already matured or otherwise termed and the prior debt was used for an eligible business purpose (i.e. not used for any of the prohibited activities and uses listed under Sections 3 and 5 above); and
 - iv. The new credit has not been extended for the sole purpose of refinancing existing debt owed to that same Participating Lender.

- b. **Ineligible Debt:** The loan must not be made in order to place under the protection of the DCCSP prior debt or investment that is not covered under the DCCSP.