

MINUTES OF THE
NEW MEXICO SMALL BUSINESS INVESTMENT CORP.

May 23, 2014

A meeting of the New Mexico Small Business Investment Corporation was called to order on this date at 9:00 a.m. in the conference room of WESST Enterprise Center, 609 Broadway Boulevard, N.E., Albuquerque, New Mexico.

A quorum was present:

Members Present

Ms. Roxanna Meyers, Chair

Mr. Alan Fowler, Vice Chair

Mr. Joseph H. Badal, Past Board Chair

Mr. Lupe Garcia

Mr. Steven E. Morgan, Secretary/Treasurer [by telephone]

Mr. Clarence L. Smith [designee of Hon. James Lewis, State Treasurer] [by telephone]

Members Excused

Ms. Launa Waller

Financial Adviser to Board

Mr. Russell Cummins

Board Legal Counsel:

Mr. Randy McDonald

Recording Secretary:

Ms. Judith Beatty

Guests Present:

Mr. Mike Doolittle, NMMP

Mr. Lynn Carrozza

Mr. Richard Harding

Mr. David Boland

REVIEW AND ACCEPTANCE OF AGENDA

Mr. Badal moved to accept the agenda, as presented. Mr. Fowler seconded the motion, which passed unanimously by voice vote.

REVIEW AND ACCEPTANCE OF BOARD MINUTES

Mr. Smith moved approval of the February 17, 2014, minutes, as submitted. Mr. Badal seconded the motion, which passed unanimously by voice vote.

FEBRUARY THROUGH APRIL 2014 FINANCIAL REPORTS

Mr. Cummins stated that the February and March financial statements were emailed to Board members.

Mr. Cummins commented that several different equity funds posted profits in March, the largest from Verge Fund's sale of ZTEC.

Mr. Cummins reviewed the status of ACCION and The Loan Fund as of 4/30. He noted that ACCION has about \$3.8 million drawn against the NMSBIC's \$5 million commitment, and The Loan Fund is at \$7.2 million versus the \$10 million commitment. Based on activity for the past six months, ACCION has about 12 months of room and The Loan Fund has about 13 months. He said he would review these funds in December to determine whether an increase would be appropriate at that time.

Chair Meyers discussed her concerns over ACCION's ability to continue its lending with a larger portfolio and without additional staff who have the specialized skills required for this type of lending activity.

Mr. Badal commented that both ACCION and The Loan Fund are better organizations today than they were two years ago, and he is impressed with what they are doing to satisfy their mission and get money out to small companies around the state.

Mr. Fowler moved to accept the financial reports for February through April 2014. Mr. Garcia seconded the motion, which passed unanimously by voice vote.

PROPOSED NEW LENDING PARTNER, NEWCO LLC

Appearing before the Board were Mike Doolittle, Managing Partner, New Mexico Mezzanine Partners; Lynn Carrozza, proposed LLC managing member; and Richard Harding and David Boland, proposed LLC members. [Proposed LLC member Dorian McKenzie was not present.]

Mr. Doolittle stated that the prospective principals of NewCo (an entity which has not yet been formed) are proposing that the NMSBIC provide a loan facility to NewCo. Its purpose would be to provide loans to businesses throughout New Mexico in a similar fashion to the debt facilities that have been provided to New Mexico-based companies by New Mexico Mezzanine Partners for the past six years.

Mr. Doolittle stated that Lynn Carrozza would lead the team in this effort. Mr. Carrozza has been a limited partner in NMMP since its inception, is a member of the NMMP Investment Committee, and is a co-investor in two of NMMP's portfolio companies.

Mr. Carrozza stated that NewCo would provide growth capital to New Mexico companies not being serviced by traditional banking sources. It would target firms with competent management, adequate margins, proven growth capacity, and which demonstrate a demand for unique products and services. Growth of these companies would involve mostly hiring skilled employees who demand higher than average New Mexico wages, e.g., engineers and salespeople. For many of the companies being targeted, the revenue comes from outside of New Mexico, so NewCo hopes to also build the economic base in New Mexico.

Mr. Carrozza said a team has been assembled to provide due diligence and analysis of prospective companies and to negotiate terms. NewCo would actively be engaged on a monthly basis with monitoring and supporting the strategy and operations of these companies.

Mr. Carrozza stated that NewCo would be providing sweat equity – they would be paid after the NMSBIC gets its money back, with a return. The only potential exception is if they raise more capital after this initial demonstration and develop a portfolio. One of their members, Dorian McKenzie, who will be providing monthly communication reports and bookkeeping services, may deserve a stipend later.

Mr. Carrozza noted that, other than a requested quarterly \$5,000 reimbursement for NMSBIC requirements to provide all audit and quarterly reporting services, all NMSBIC funding would go directly to the portfolio companies.

Mr. Carrozza stated that Exhibit III of the materials describes four prospective portfolio companies. He said some are ready for funding now, while others are 6 to 12 months away from that point. Loans to the prospective portfolio companies would be in the \$500,000 to \$1.5 million range.

Responding to Mr. Fowler, Mr. Harding said they would expect to see 6 to 10 quality (cash flow positive) deals a year.

Mr. Doolittle stated that he would not be involved in NewCo.

Mr. Carrozza said NewCo is requesting \$750,000 from the NMSBIC to fund one company within the context of the proposed term sheet.

Mr. Carrozza responded to questions from Chair Meyers about the proposed portfolio companies.

Chair Meyers asked if anyone has sat down with banking community representatives to discuss the need for this type of lending in New Mexico and ways that might be accomplished. She wondered if enough pressure has been put on these banks to step up and help out.

Mr. Harding responded that they have had “lots of meetings with most of the banks” in terms of their role in building a company, but banks are very reticent to lend all over the country right now. Even in the best of times, before the banks got into trouble, it was not an easy task to get commercial lenders to understand why a mezzanine entity or lending group was important to their portfolio. He added that, in some conversations with the banks, mezzanine lenders were viewed as competition.

Mr. Carrozza said all the loans would be secured. Three of the four companies have been in business for several years. Where there is a banking relationship, it would be subordinate to the senior bank debt. With no banking relationship, the loans would be secured by hard assets or intellectual property.

At Mr. Badal's request, Mr. Carrozza discussed the company being targeted for the \$750,000 in funding, as well as terms. The company has been profitable for a number of years and is poised for significant growth.

Mr. Harding stated that the NewCo team will be able to handle a fairly robust amount of capital, depending on deal flow, and they look forward to more deals than this one.

Mr. Badal commented that, once there is anecdotal evidence of a successful transaction, NewCo should be able to take quality deals to community banks around New Mexico and point out that they are not competitors.

Mr. Cummins said the NMSBIC has about \$2.7 million invested in New Mexico Mezzanine Fund, which ends September 2015. In his discussions with the principals of NewCo, one concept is that, as the \$2.7 million starts coming back, NewCo's line of credit might be increased if the demonstration fund is successful. He noted that the NMSBIC has about \$3 million in available capital at the current time.

[Representatives left the room.]

Chair Meyers suggested that the Board discuss whether this is the highest and best use of taxpayer money, given the likelihood that other investors are waiting in line to lend money to this company; or should the NMSBIC be reaching out to community banks and showing them where the available funding is.

Mr. Badal responded that it is not the NMSBIC's job to find funding beyond its own funding capabilities.

Mr. Badal commented that, of the four prospective portfolio companies, only the one being proposed for funding is EBITDA positive. NewCo would expect the NMSBIC to provide the funds to make them cash positive, which sounds like venture capital, and he therefore would not want to fund them. With respect to the first deal, however, Mr. Badal pointed out that the NMSBIC has been encouraging NMMP to do this kind of thing for at least two years.

Mr. Badal said he would vote to approve the \$750,000 request with the contingency that the NMSBIC would only look at cash flow positive businesses, and that NewCo would show the NMSBIC a "case study" of how these deals would look. He said he would not approve the \$5,000 fee.

Mr. Cummins suggested that the NMSBIC could find itself competing with banks if it wants deals that have been cash flow positive for two or three years. In discussion with NewCo representatives, they have said they are looking at companies that are almost cash flow positive.

Chair Meyers commented that the NMSBIC would essentially be creating another bank to replace the banks that will not do mezzanine lending. If the NMSBIC's goal is to increase jobs and get money into the hands of good entrepreneurs, she wondered if there is a less expensive and more efficient way to do this, i.e., is there an entity with an infrastructure in place to provide this kind of financing.

Mr. Cummins said the five loans in the New Mexico Mezzanine Fund are the kinds of loans that NewCo anticipates doing.

Mr. Badal moved to approve the \$750,000, subject to receiving more information; and that they provide a term sheet that is clearer than this one for this deal; and that NewCo can make loans based only on the parameters set out in the term sheet.

Mr. Badal also moved that Mr. Cummins work on the parameters and finalize them for review.

Mr. Badal also moved that there be no future advances for subsequent deals until the previous deals have become positive.

Mr. Fowler seconded the motion.

Chair Meyers moved an amendment that the NMSBIC be informed of how deals are structured, including all of the terms of the deal; and that the NMSBIC's interest should be stated as a percentage of the borrower's interest.

The amendment was accepted as friendly.

Mr. McDonald noted that the Collateral paragraph in the term sheet states that the proposed loan would be secured by the promissory notes related to the underlying portfolio company loan. He said he saw no reason why the NMSBIC's loans to them should not be secured by at least all of the collateralized documents.

Board members agreed.

Mr. Badal withdrew his motion for approval.

Mr. Badal moved to approve the \$750,000 request, but that it be subject to authorizing Mr. Cummins to negotiate terms that satisfy security, collateral issues and compensation issues; that the \$5,000 not be paid; and that the NMSBIC is not making any commitments to any additional deals. Mr. Fowler seconded the motion, which passed by voice vote, with Chair Meyers voting against the motion.

**NM GAP FUND, CLARIFICATION REGARDING NEW INVESTMENTS:
CHRIS TRAYLOR, VENTURE PARTNER**

Mr. Cummins stated that the NMSBIC Board approved changes to the NM Gap Fund Limited Partnership agreement at the last meeting to 1) allow a \$50,000 management fee for one year, and 2) allow an increase in fund expenses from \$8,000 to \$16,000 for one year.

Mr. Cummins noted that the NM Gap Fund partnership agreement prohibits capital calls for new investments beyond the third anniversary (December 31, 2012), but does not appear to prohibit new investments after the third anniversary. He said the NM Gap Fund management believes there are new investment opportunities worthy of additional due diligence, but recognize that investments in new

companies might not follow the spirit of the agreement. On April 3, he, Mr. Badal and Mr. Morgan met with Chris Traylor, venture partner with Flywheel Ventures, who discussed possible new investment opportunities and asked to appear before the Board to seek guidance as to whether he should allocate his time to due diligence of new investment opportunities.

Mr. Traylor said he wanted to be sure he had the Board's "blessing" to proceed with any new investments. He stated that he had provided the Board with four redacted summaries of companies that represent some high quality investment opportunities in New Mexico. He said the investments he is contemplating are of high quality and are in the "intermediate stage" of due diligence, and he believes these companies can experience exits within the life of the fund.

Mr. Traylor said this money can be used for either follow-on investments into existing portfolio companies, or it can be set aside for future management expenses. Otherwise, the money would be returned to NMSBIC. With NM Gap Fund, they are limited from investing more than 10 percent of the total fund in any one company, and they are also precluded from providing follow-on capital to companies that leave the state. Mr. Traylor said the plan is to work closely with the companies, take a board seat in some cases, and instill confidence in out-of-state investors to invest their money. He said he feels this will be the case with at least one of the four companies NM Gap Fund is doing due diligence on now.

Mr. Cummins noted that NM Gap Fund has a little over \$2 million, with about \$425,000 to deploy (after expenses), so has a maximum of about \$200,000 to invest in any one company. Mr. Traylor said he would make one to two more investments.

Chair Meyers asked Mr. Traylor if he would agree to not invest NMSBIC money in any company where NMSBIC already has money invested. Mr. Traylor responded that this could prevent him from putting money toward the highest quality investment opportunity. He said he has a responsibility to maximize a return profile as well as NM Gap Fund's economic development objective.

Mr. Cummins said NMSBIC cannot own more than 49 percent of the common stock of a company, which is a legislative requirement.

Chair Meyers and Board members thanked Mr. Traylor for his presentation, and agreed that there were no limitations in the LP agreement that would preclude him from moving forward in continuing his due diligence with the goal of making additional investments.

BUDGET FOR FISCAL YEAR ENDING JUNE 30, 2015

Mr. Cummins recommended approval of the NMSBIC budget.

-- Interest income is proposed at about \$315,000, up from projected 2013-2014 interest income of approximately \$291,000.

-- Total operating expenses are proposed at \$251,715, up from projected 2013-2014 operating expenses of \$241,000. While legal expenses this year came in under budget at \$13,000, \$18,000 has been budgeted to allow for adequate legal services.

-- Net income from operations is proposed at \$62,869.

Mr. Badal moved to accept the budget. Mr. Fowler seconded the motion, which passed unanimously by voice vote.

CONTRACT RENEWALS

a. Professional Services Contract: Legal

Mr. Cummins recommended approval of this contract with Randall J. McDonald for one year from July 1, 2014 to June 30, 2015. There is no proposed change in the hourly rate of \$198, and no changes to other terms.

Mr. Garcia moved for approval. Mr. Fowler seconded the motion, which passed unanimously by voice vote.

b. Professional Services Contract: Board Minutes

Mr. Cummins recommended approval of this contract with Judith Beatty for one year from July 1, 2014 to June 30, 2015. Her request is to increase the hourly rate from \$46 to \$48, with no changes to other terms.

Mr. Badal moved for approval. Mr. Garcia seconded the motion, which passed unanimously by voice vote.

SHORT TERM INVESTMENTS, \$1.5 MILLION ONE-YEAR CD INVESTMENT

Mr. Cummins stated that NMSBIC has a \$1 million CD, plus interest, that matures on June 9, 2014 at First National Bank of Santa Fe. He recommended withdrawing \$500,000 from the FNB SF money market account, add to the \$1 million plus interest from the maturing CD, and invest approximately \$1.5 million for 1 year at FNB SF at a rate of approximately 0.45 percent. Rates are subject to change at the time the CD investment is made.

Mr. Badal moved for approval. Mr. Garcia seconded the motion, which passed unanimously by voice vote.

INSURANCE RENEWAL, DIRECTORS & OFFICERS POLICY

Mr. Fowler moved for approval. Mr. Garcia seconded the motion, which passed unanimously by voice vote.

COMMUNITY OUTREACH & BOARD MEETING, DATE FOR OCTOBER 2014 MEETING

Mr. Cummins stated that he would work with Ms. Waller on a convenient date and then coordinate with Board members.

BOARD CONTINUING EDUCATION, NMSA 7-27-5.15

Mr. Cummins stated that, at the time funding was first provided to NMSBIC from the Severance Tax Permanent Fund, the balance was approximately \$4.7 billion and the NMSBIC received a distribution of \$47 million, or 1 percent. After a decline in value, as of February 28, 2014, the fund had grown to \$4.49 billion. Following distribution of about \$200 million to the general fund, the balance of the fund could go down to roughly \$4.29 billion. If the balance of the fund increases above \$4.7 billion, NMSA 7-27-5.15 will result in additional funds provided to the NMSBIC based on 1 percent of the balance of the fund.

INVESTMENT POLICY, INVESTMENT GRADE CORPORATE BONDS AS COLLATERAL

Mr. McDonald stated that, at the last meeting, he was asked to look into whether the NMSBIC could buy CDs that have collateral investment grade corporate securities. He said the NMSBIC's Investment Policy, which tracks the NMSIC's, does not include investment grade corporate securities. While the NMSBIC is not a state agency, it clearly has state funds, and the statute says that state funds may not be invested in this way.

ANNUAL CERTIFICATION FORM

Mr. Cummins said the Board suggested that the NMSBIC have an annual certification to be signed by each of its partners at the end of each fiscal year. He said he has drafted a form and submitted it to Mr. McDonald for review.

EXECUTIVE DIRECTOR/INVESTMENT ADVISOR REPORT

-- The balance under the Prior Agreement with Accion has dropped to \$2.8 million, and the balance under the 2013 lending program has increased to \$1.1 million. Accion's combined outstanding balances are at 79 percent of its \$5 million maximum funding amount.

-- The Loan Fund's balance has increased to \$7.2 million, which is 72 percent of its \$10 million maximum funding amount. At this time, The Loan Fund has not yet originated any loans greater than \$350,000 with NMSBIC funds.

-- Loan documents for a \$1.5 million unsecured revolving line of credit with the New Mexico Mortgage Finance Authority have been signed. NMSBIC is awaiting a Secretary's Certificate documenting an MFA Board Resolution authorizing the transaction.

-- WESST's loan balance has increased to \$60,760. Its outstanding balance is at 18 percent of its \$375,000 maximum funding amount.

CHAIRMAN'S COMMENTS


Chair Meyers asked Mr. Cummins to meet with the Holly Company to discuss ideas for alerting business owners and entrepreneurs in the Clovis area about the NMSBIC's community outreach event in October.

Responding to Chair Meyers' comments about the need for the banking community step up and participate in lending to entrepreneurs and small businesses, Mr. Badal suggested that she contact the New Mexico Bankers Association and schedule an appearance at one of their meetings.

Mr. Cummins noted that The Loan Fund is working on building a better relationship with the 20 SBDC offices around the state, and have a goal of getting one referral from every office each quarter. They have also set up videoconferencing with every SBDC office in the state.

ADJOURNMENT

Its business completed, the NMSBIC Board adjourned the meeting at 11:45 a.m.



Roxanna Meyers, Chairman and President

7-18-14

Date