

MINUTES OF THE
NEW MEXICO SMALL BUSINESS INVESTMENT CORP.
REGULAR MEETING

February 27, 2012

A regular meeting of the New Mexico Small Business Investment Corporation was called to order on this date at 8:05 a.m. in the conference room of the WESST Enterprise Center, 609 Broadway Blvd., N.E., Albuquerque, New Mexico.

A quorum was present:

Members Present:

Mr. Joseph H. Badal, Chair [by telephone]
Mr. Sam Cobb [by telephone]
Mr. Alan Fowler, Secretary/Treasurer
Mr. Lupe Garcia
Ms. Roxanna Meyers, Vice Chair
Mr. Clarence L. Smith [designee of Hon. James Lewis, State Treasurer]
Ms. Launa Waller [by telephone]

Members Excused:

None.

Legal Counsel to Board:

Mr. Randy McDonald

Financial Advisor to Board:

Mr. Paul Goblet

Recording Secretary:

Ms. Judith Beatty

Guests Present:

Mr. Chad Cooper, NM African American Chamber of Commerce

APPROVAL OF AGENDA

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

REVIEW AND ACCEPTANCE OF BOARD MINUTES: January 23, 2012

Mr. Cobb moved approval of the January 23 Minutes, as submitted. Mr. Fowler seconded the motion, which passed unanimously by voice vote.

REVIEW AND ACCEPTANCE OF FINANCIAL REPORT

Mr. Goblet reviewed the January financials. He said the figures are essentially unchanged from December's financial report (with the exception of a small capital call) because the fourth quarter reports haven't yet been received from the equity partners.

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

PRE-PRESENTATION DISCUSSION ON NM MEZZANINE FUND: REVIEW OF FUND ECONOMICS

Vice Chair Meyers said she emailed members an analysis of investments made in the New Mexico Mezzanine Fund. In short, the entire fund has spent \$750,000 in management fees and \$3.125 million of capital has been deployed, and the question is what the NMSBIC can do to get more money deployed to people who can benefit from it and which can benefit the state.

Mr. Goblet agreed that the 4% management fee is high. He said the thought process in creating this fund was that, if it could deploy two-thirds of its capital -- \$4 million -- and have that capital outstanding, that would have generated \$400,000 to \$500,000 a year, which would have offset all of the management fees. He said this fund is unique in that it charges interest on the capital, so while the management fee percentage is higher, this is the same structure of 200 funds that the SIC has invested in. The difference is that the SBIC funds are significantly smaller.

Vice Chair Meyers said she agrees with the NM Mezzanine Fund's request to relax their lending requirements, making them more reasonable for today's market, because it would allow them to deploy the rest of their fund and lower the management fees.

Noting that the NM Mezzanine Fund has asked to amend the lending guidelines in the LP agreement, Vice Chair Meyers suggested the Board consider also amending the agreement to lower their management fee.

Mr. Goblet responded that the only amendment to the LP agreement, which is the contract, would be the ability to invest the capital for another six months because their investment time has ended. Outside of the LP agreement there is a freestanding investment policy, which would be relaxed so the capital could be deployed.

Vice Chair Meyers asked Mr. McDonald if the Board could legally lower the management fee when it opens up the LP agreement for amendment, and Mr. McDonald responded that the Board could try to negotiate a lower fee.

Chairman Badal and Vice Chair Meyers noted that NM Mezzanine Fund wants to raise money for a second fund and will be approaching the NMSBIC, and this would also offer an opportunity to negotiate.

Chairman Badal commented that, considering today's lending environment, the NM Mezzanine Fund would seem very well positioned to become a successful fund. At the time the fund was created, there was no other mezzanine fund in New Mexico to serve as a model, and to some degree the agreement was flawed. He said the NMSBIC now has an opportunity to go back and fix that.

Chairman Badal suggested that a subcommittee of the Board meet with the NM Mezzanine Fund and hash out a plan that could be brought to the March NMSBIC meeting for action.

**PRESENTATION FROM NM MEZZANINE FUND:
DISCUSSION AND POSSIBLE VOTE TO AMEND LPA**

NM Mezzanine Partners representatives Mike Doolittle and David Boland appeared before the Board and presented their proposal to change the fund's investment period and NMMP guidelines.

- The GP proposes an amendment to the Partnership Agreement that would extend the investment period of the fund by one additional year to September 25, 2012.
- The GP proposes an amendment to the Partnership Agreement that would modify the investment guidelines to reflect a two-tiered structure:

Current investment guidelines:

- NM based.
- Annual revenues of at least \$1 million.
- Achieved positive EBITDA and reasonably project future EBITDA margins of at least 5%.
- Demonstrated debt service capability.
- Reasonable prospects to retire at least 50% of their senior indebtedness within three to five years of the initial investment.

Proposed investment guidelines

For first lien notes (where NMMP is a senior secured lender)

- NM based.
- **Achieved positive EBITDA or the ability to achieve positive EBITDA within 18 months based on realistic financial projections.**
- **Demonstrated debt service capability or projected ability to service debt commensurate with realistic EBITDA projections**
- Reasonable prospects to retire at least 50% of their senior indebtedness within three to five years of the initial investment.

For subordinated notes (where NMMP's position is subordinate to a bank)

- NM based.
- Achieved positive EBITDA and reasonably project future EBITDA margins of at least 5%.
- **Demonstrated debt service capability or projected ability to service debt commensurate with realistic EBITDA projections**
- Reasonable prospects to retire at least 50% of their senior indebtedness within three to five years of the initial investment.

Responding to Vice Chair Meyers, Mr. Doolittle said legal expenses for each of the two loans currently outstanding have been no more than \$15,000.

Mr. Doolittle discussed the status of the current investments, projected performance and the composition of the portfolio. He said invested capital would be diversified across five industries (financial services, life science, internet technology, engineering and agriculture) and distributed fairly evenly.

Chairman Badal asked Mr. Doolittle how many possible deals there would be if the Board were to approve the requested changes.

Mr. Doolittle responded that, with respect to the three deals currently sitting in the pipeline, all have excellent management teams and it has taken a while to identify them, work with them and negotiate terms, but he would estimate there are two to three times this number out there that are looking for growth capital.

Responding to Vice Chair Meyers, Mr. Boland said the interest rate varies, depending on what is negotiated with each deal. Mr. Doolittle added that the rate is 9-15%.

Chairman Badal noted that, when he and Mr. Fowler met with Mr. Doolittle a few days ago, they raised the question about lowering the interest rate and how many more deals might fall into their lap if they were approaching this on a different investment return basis – would it be

possible to reinvent the concept of mezzanine through changing the investment terms and thus creating more opportunities.

Vice Chair Meyers asked Mr. Doolittle what effect, if any, there would be on the three potential deals if the Board were to take longer than a month to take action on their request, and Mr. Doolittle responded that one deal would no longer be there.

[Messrs. Doolittle and Boland left the proceedings.]

Action was deferred to later in the meeting.

DISCUSSION AND POSSIBLE VOTE ON SHORT-TERM DEPOSITS

Mr. Goblet stated that, in response to Board direction, he has continued to search for local banks that will provide 100% collateralization. He said the NMSBIC has \$6,780,646 maturing on March 8 in the CDARs program at New Mexico Bank & Trust.

Based on the rates quoted in his report, Mr. Goblet recommended that the Board place \$3 million in deposits at New Mexico Bank & Trust at .20 basis points for 6 months and \$3.5 million at First National Bank of Santa Fe at .35 basis points for 12 months. He said this would begin laddering the NMSBIC's money and would service all of the forecasted capital calls. He said both deposits would be 100% collateralized with US Government securities.

Mr. Goblet said the remaining \$200,000 should be deposited at US bank in their "non interest bearing" money market account, which is fully insured by the FDIC and currently pays .20 basis points.

Mr. Badal so moved. Mr. Fowler seconded the motion, which passed unanimously by voice vote.

ADVISOR'S REPORT

Management fees and expenses

Mr. Goblet reviewed an outline of the management fees paid by NMSBIC to date, as well as remaining management fees that would be payable over the remaining life of the funds.

Mr. Goblet noted that, from 2003 to 2011, there was a total of \$4.3 million paid in management fees and a total interest income of \$5.6 million. Management fees in 2012 are forecasted at \$505,000 and earned income is expected to be \$270,500.

New Mexico Community Capital

Mr. Goblet said two investments will be meaningful drivers of fund returns, Aspen Aviation and IntelliCyt; and the key to getting decent returns will be to recapture all other invested capital from some of the less successful companies in the portfolio.

Flywheel NMSBIC I

Mr. Goblet stated that the Flywheel Ventures Advisory Committee met on February 21 and re-approved the valuation policy and the related valuation of the portfolio at year-end.

Mr. Goblet said Flywheel I shows positive cash on cash value and a positive net IRR. He noted that one investment, Astria, makes up over 72% of the value of the Fund due to its operating success and likely sale value, which is over a 5x investment capital.

Mr. Goblet said Flywheel-NMSBIC I has four investments in New Mexico companies. He said \$1,036,405 has been invested in these companies with a present valuation of \$435,000. While Miox's valuation represents 11% of Flywheel I, it is 71% of the valuation in Flywheel-NMSBIC I. Mr. Goblet said a typical fund has to generate a 1.5-to-1 cash-on-cash return in order to offset all fees and expenses over the 10-year life of the fund. He said he seriously doubted that this fund would generate a positive return to the NMSBIC, although Miox has attracted \$50 million of equity capital, employs 50 to 60 people, and has just attracted a \$5 million strategic equity investment from Schlumberger to develop water filtration systems for the oil and gas drilling sector.

Mr. Goblet reviewed a Flywheel I financial overview, including key financial metrics and the GP's outlook as of February 2012 on portfolio rankings.

Verge Fund and Verge Fund II

Mr. Goblet reported that TruTouch Technology just closed on a \$3 million round of new equity capital, of which Verge provided a small follow-on investment from Verge I and I.5. This new capital, together with a large grant, will hopefully carry the company through its next product development stage.

Mr. Goblet said Verge II has made a follow-on investment in one of its portfolio companies and expects to make a new investment in the next few weeks.

NM Growth Fund (NMBBH issue)

Mr. Goblet stated that Mesa Ventures will put forth a formal extension of the limited partners' ability to opt into their pro rata portion of OneConnect IP/SkiWi, now called Agave Broadband. He said the Board should consider whether it wants to commit another \$17,000 -- the NMSBIC's pro rata portion of that subscription as a member of New Mexico Growth Fund I -- understanding that the benefit is that the Board will have the ability to monitor this company's

progress and six months from now consider whether it makes sense to put any additional capital into the company.

ACCION

Mr. Goblet noted that ACCION is beginning to see an increase in loan volume and has initiated an effort to seek larger, high quality clients, believing this will lead to an increased portfolio size for the remainder of the year. He said they anticipate visiting with the NMSBIC Board toward the end of 2012 to request an increase in the facility.

Mr. Goblet said ACCION began implementing a new policy put forth by the ACCION Network, calling for the automatic write-off of any loan greater than 180 days past due, even if a client had submitted payments during the month. He said ACCION was forced to write off \$34,000 worth of loans in January, a far higher amount than is typical.

WESST Corp

Mr. Goblet reported that WESST Corp has a very small loan balance outstanding at \$52,000. They have added an experienced part-time lender, which should lead to more loan volume.

Mr. Goblet said WESST Corp wrote off a loan last month, but will have a sale on a portion of the collateral (a car), which will result in a small collection of possibly \$3,500.

The Loan Fund

Mr. Goblet said The Loan Fund only reports quarterly. They are expected to make a \$500,000 capital call in early March, which will require them to provide a stub period lending report and show compliance with all covenant ratios.

New Mexico Angels

Mr. Goblet said Board members have been forwarded an invitation to a New Mexico Angels lunch in Albuquerque on March 1 at 11:30 at Gianni's, and asked them to advise him if they wish to attend.

Consolidated financials – NMSBIC - chronology

Mr. Goblet distributed and reviewed the NMSBIC's financials dating back to 6/30/2002.

DISCUSSION ITEMS

a. Proposal from Mesa Ventures Regarding NMBBH

This item was deferred, pending receipt of a formal proposal from New Mexico Broadband Holding.

b. Discussion Regarding RFP for Financial Advisor

Vice Chair Meyers reported that she and Chairman Badal worked with Mr. McDonald and Mr. Goblet in looking at the last RFP that went out, and made some recommendations, which will be shared with Board members. She said the RFP will be issued in March, and she, Chairman Badal and Mr. Cobb have agreed to vet the proposals and winnow the field down to two finalists.

NEW MEXICO MEZZANINE FUND DISCUSSION (Cont'd)

Vice Chair Meyers said she felt management fees should be performance based going forward.

Chairman Badal moved to approve New Mexico Mezzanine Partners' request to extend the investment term, and to amend the underwriting criteria to allow them more flexibility; in return, their management fee going forward would be based on a pro rata basis of funds deployed to the \$6.2 million total amount of the original fund; so if they only get \$3.1 million deployed, they would only get 50% of the management fee and if they get \$6.2 million out, they would get 100% of the management fee to the maximum of \$250,000 a year.

Mr. Fowler seconded the motion.

Responding to Mr. Cobb, Mr. McDonald stated that their maximum fee is \$250,000 per year for the next three years, and the NMSBIC's share is 40%. In order to amend the agreement, it would take a 66-2/3% vote of the partnership interest to amend it, so it would take the NMSBIC and at least one other of the larger limited partners, and it would also take the approval of the general partner.

Mr. Fowler said the interim subcommittee suggested by Chairman Badal earlier in the meeting would be more suited to developing criteria for a new investment round and negotiating a fair management fee along with incentives, etc. Right now, he likes Chairman Badal's motion because the Board has enough sense about what is going on that it doesn't need to spend more time discussing the extension and the ability to change the fee.

Chairman Badal agreed with Mr. Fowler.

Vice Chair Meyers commented that, in hindsight, this experience seems to indicate that New Mexico may not be ready for equity funds or even a separate mezzanine fund. She said all of the large banks already have mezzanine funds; and while they may not be paying any attention to New Mexico, perhaps the NMSBIC can negotiate with some of them. She said the NMSBIC is spending a lot of money trying to deploy this money.

Mr. Fowler proposed an amendment that the management fee would go to a pro rata basis effective on April 1.

The amendment was accepted as friendly.

The motion passed unanimously by voice vote.

FINALIZATION FOR MAY BOARD MEETING AND PUBLIC PRESENTATION


The Board agreed to hold the May meeting in Hobbs.

Mr. Badal moved that Mr. Goblet go to Hobbs and do the initial planning for the May meeting. Mr. Garcia seconded the motion, which passed unanimously by voice vote.

NEXT MEETING: Monday, March 26, 2012, WESST Enterprise Center

ADJOURNMENT

Its business completed, the NMSBIC Board adjourned the meeting at approximately 10:35 a.m.



Joseph Badal, President

MARCH 26, 2012

Date