

STATE OF MINNESOTA
MINNESOTA ENERGY AND ECONOMIC DEVELOPMENT AUTHORITY

In the Matter of the Proposed Rules
Governing Loan Application Procedures,
Tourism Fund Loans

STATEMENT OF NEED
AND REASONABLENESS

I. The Minnesota Energy and Economic Development Authority (Authority) presents herein facts and justifications establishing the need for and reasonableness of its proposed rules governing loan application procedures. Tourism Fund Loans. These proposed permanent rules are similar to the existing emergency rules for tourism loans. Minn. Rules 8300.3060-8300.3070 [Emergency].

II. Impact on small business. Under the Emergency Rules the Authority has approved participation in 43 tourism loans. The total amount of the loan participation approved by the Authority is approximately \$1.2 million. Attached as exhibit A is a map showing the locations of the tourism businesses for which loan participations have been approved. The Authority's authorizing legislation directs that their powers be used for small business purposes. The Authority manages several loan programs and is able to help qualified small businesses through the loan guarantees, loan participations, or outright loans. The proposed tourism rules do not establish a regulatory compliance or reporting program with mandatory application. The rules prescribe policy and procedures for the operation of a benefit program, and the decision to participate in a financial assistance program is voluntary. A tourism business can elect to participate in a financial assistance program, and that decision can be made for each individual transaction.

In terms of compliance and reporting requirements, because the Authority operates benefit programs, rather than regulatory programs, it operates on eligibility rather than compliance requirements. However, the Authority has adopted the least stringent eligibility requirements consistent with statutory authorizations of the programs. For example "eligible borrower" is defined to refer to targeted small businesses which are smaller businesses. The proposed rules do not contain any design or operational standards.

As previously discussed, the financial assistance programs are aimed at targeted small business. All of the proposed rule requirements are promulgated with the capabilities and needs of smaller businesses in mind. The requirements adopted in the rules are those minimal and necessary to fulfillment of statutory requirements and standards; further exemptions are neither appropriate nor authorized. It should be noted that because these rules will govern a benefit program for only the Tourism Industry, the Authority has made special efforts to make all known tourism businesses aware of the proposed rules. In addition to mailing the Notice of Intent to Adopt the Rules to those individuals on the rulemaking notice list, the Authority will mail the Notice of Intent to Adopt these Rules to the approximately 2000 Tourism businesses known to the Minnesota Office of Tourism.

III. Discussion of Proposed Rules. For the convenience of the reader, the proposed text of the rule is set forth followed by the section of the Statement of Need and Reasonableness which relates to the proposed section of the rule set forth.

8300.3060 PURPOSE OF TOURISM LOAN PROGRAM

The purpose of the tourism loan program of the Authority is to provide loans to upgrade and improve Minnesota's small tourism businesses. This program would match loans by local financial institutions, share credit risks, and provide for lower interest rates than are otherwise now available.

8300.3060 PURPOSE OF THE TOURISM LOAN PROGRAM

Parts 8300.3060 to 8300.3070 pertain to the tourism loan program. Under Minnesota Statutes, section 116M.08, subd. 4 the Authority can adopt rules. These program specific rules outline the parameters and requirements unique to this program. The program is defined as the provision of financial assistance by purchasing a participation in a loan made to an eligible tourism business for an eligible tourism project. By purchasing a participation with funds from the Economic Development Fund, the Authority will, in partnership with Minnesota private lending institutions, increase the amount of money available for loans to the State's tourism business. The tourism loan program will also reduce the effective cost of borrowing to tourism businesses. The borrower has a lower effective interest rate because the Authority participates in up to 50% of a loan made by private lending institutions. This participation is at a lower interest rate than the lending institution, thereby lowering the overall rate of interest from what it would have been without the program.

8300.3061 DEFINITIONS

Subpart 1. Statutory terms. The definitions in Minnesota Statutes, section 116M.03 and this part apply to parts 8300.3060 to 8300.3070.

Subpart 2. Act. Act means the Minnesota Energy and Economic Development Authority Act.

Subpart 3. Commissioner. Commissioner means the commissioner of energy and economic development.

Subpart 4. Eligible borrower. Eligible borrower means a person, partnership, firm, or corporation engaged in, and determined by the Authority to constitute a tourism business as defined by the standard industrial classification (SIC) codes 7011 and 7033 is a targeted small business. Any person to whom a loan has been made under parts 8300.3060 to 8300.3070 must maintain the (SIC) code classification as approved by the Authority throughout the loan.

8300.3061 DEFINITIONS

It is necessary and reasonable to tell readers definitions involved in these rules and what the eligibility criteria are for the program. The definition of an eligible borrower to be tourism business as defined by the Standard Industrial Classification (SIC) code is consistent with the Authority's other programs which also use that same regulation. Under Minnesota Statutes 116.03, subd. 4 (1984), "eligible small business" considered to be eligible under the regulations of the United States Small Business Administration (SBA) pursuant to United States code, title 15, sections 631 to 647. The SIC code found at 13 CFR is a regulation of the SBA. We note that the Minnesota Supreme Court has expressly held the incorporation of SBA definitions as to eligible small business is not an unconstitutional delegation of state legislative power to the federal government. See Minn. Energy and Economic Development Authority v. Printy, 351 N.W. 2d 319, 351 (Minn. 1984). The SIC codes listed in the rules are the most appropriate SIC codes for the tourism businesses. It is also important to note that SIC codes are widely used by commercial lenders in classification of businesses.

It is also reasonable for the Authority to limit the program to target small businesses as defined in Minnesota Statutes §116.03, subd. 8 (1984). Targeted businesses are defined to be very small businesses. Typically it is the smaller tourism businesses which have the most difficulty obtaining financing and are most in need of assistance. According to officials at the Minnesota Office of Tourism, "most tourism businesses throughout the state were built in the 1930's, 40's, and 50's and are in desperate need of improvements and renovation. Of these businesses, 75 to 80 percent have gross sales under \$150,000 thereby making it difficult to obtain financing". Since it is the smaller tourism businesses which are most in need of assistance it is reasonable for the Authority to use it's limited funds to those businesses with the greatest need. Moreover, the legislature has specifically directed the Authority to "make every effort to assure that at least 50% of the loans made or purchased by the Authority in each fiscal year consist of loans with a principal amount of \$100,000 or less to targeted small businesses." Minnesota Statute §116M.07, subd. 10 (1984). By establishing a program designed only for "targeted small

businesses" the Authority is implementing the directive of the legislature and helping to assure that "targeted businesses" receive financial assistance from the Authority instead of having all the financial assistance go to larger businesses.

8300.3062 ELIGIBILITY OF PROJECT FOR TOURISM LOANS

In order to receive loan participation by the Authority, a financial institutions loan must be to an eligible borrower for an eligible cost in an eligible project. The maximum state participation is 50 percent of the project, with a maximum for any one project of \$50,000. The financial institution shall make application for participation on behalf of an eligible borrower.

8300.3062 ELIGIBILITY OF PROJECT FOR TOURISM LOANS

The eligibility requirements are needed to inform readers of the rules concerning funding under the program. The parameters are reasonable because the participation of the Authority is 50 percent of the project costs, with a maximum participation of \$50,000 on any one project, and it provides the incentive for an outside lender to participate in the financing of a project. It is possible that money to make tourism loans may be made available from other sources, i.e., for example, a federal grant, or a grant from a private foundation. When that is the case it is reasonable that the project comply with the eligible criteria required by the funding source. The limit of \$50,000 per participation helps the Authority to implement the legislative mandate set forth in Minn. Stat. §116M.07, subd. 10 that 50 percent of the loans made or purchased by the Authority be in a principal amount of \$100,000 or less.

8300.3063 ELIGIBLE PROJECT COSTS FOR TOURISM LOANS

Subpart 1. Eligible costs. Eligible costs for financing by the Authority include any costs not prohibited by subpart 2 for:

- A. building construction and improvement;
- B. site preparation;
- C. equipment;
- D. construction;
- E. engineering;
- F. authority fees including application fees of the authority; and
- G. interest due on the loan during the period of construction.

Subpart 2. Ineligible cost. Capital expenditures for project costs made more than 30 days prior to submission of an application cannot be financed with a tourism loan.

8300.3063 ELIGIBLE PROJECT COSTS FOR TOURISM LOANS

It is necessary to define for the potential applicants what is specifically meant by eligible project costs permitted under the program. The financing of building equipment and their related costs are reasonable because they upgrade and improve Minnesota's tourism industry. All of the assets listed should provide adequate collateral for our participation and for an outside lender's participation in the project financing. Such eligible costs are similar to eligible costs specified for other Authority programs, see e.g. Minn. Rules, pt 8300.3022, 8330.3042 and 8300.4017. In addition the costs listed are consistent with those costs listed as eligible under the definition of a small business loan under Minn. Stat. §116M.03, subd.19(1984).

It is necessary and reasonable to establish a cut off date for what costs are are expended. The purpose of the Authority participation is to permit tourism projects to be financed which might not have been able to go forward without Authority participation in the loan. If the Authority funded costs made more than one month prior to the application, it would be difficult to justify the proposition that the Authority funding made the tourism project possible.

8300.3064 INTEREST RATE FOR TOURISM LOANS

The interest rate on the Authority's participation under the tourism loan program is three percentage points below a full faith and credit obligation of the United States government of comparable maturity, at the time of submission of completed applications to the Authority. The Authority may, in the alternative set interest rates at a different rate after reviewing market rates and comparable sources of financing available to the borrowers at the time the financial assistance is extended.

8300.3064 INTEREST RATE FOR TOURISM LOANS

It is necessary to tell readers of the rules and what they can expect in terms of interest rates. An interest rate that is three percentage points below a full faith and credit obligation of the United States government of comparable maturity, and at the time of submission of complete applications to the Authority, is reasonable because the program provides a credit product which is not currently available through the market place. The program fills a void that helps promote economic development in the State and helps to fulfill the purposes of the Act. The interest rate set is similar to the rate set for other Authority programs. See e.g. Minn. Rules pt 8300.3033.

8300.3065 TERM OF LOAN FOR TOURISM LOANS

The maximum term of any loan will not exceed the average useful life of the real property, or 80 percent of the useful life of the equipment or machinery, or the following limits, whichever is less:

- A. for real property (land or building), ten years;
- B. for equipment or machinery, five years; and/or
- C. for a combination of items A and B, a weighted average of those years

will be used.

The financial institution is permitted to amortize the loan over a period of years up to 15 years. If the note between the financial institution and the borrower matures before the expiration of the contract between the financial institution and the Authority and the note is renewed, the contract shall remain in effect until the expiration of the contract. The Authority need not participate in the refinancing of any remaining portion of the principal not fully amortized and paid at the maturity of the contract between the financial institution and the Authority.

8300.3065 TERM OF LOAN FOR TOURISM LOANS

The indication of the term of a loan issued under the program is necessary in order to inform potential applicants about the terms. The maximum term of ten years of the useful life of the project financed, which ever is shorter is reasonable because long term financing is not available for these assets in the marketplace; therefor, the Authority's program is not in competition with other lenders in the market place. In addition, this term financing provides further incentive for an outside lender to participate in financing projects.

8300.3066 SECURITY REQUIREMENTS FOR TOURISM LOANS

All loans for real property or equipment must be secured by collateral. The financial institution must take a security interest in any collateral acceptable to the financial institution. The personal gaurantee of principal owners, officers, sole proprietors, partners, major shareholders or corporate officers of the borrower, or other related entities such as subsidiaries or parent corporations of the borrower, must also be given to the financial institution before loan participation will be approved. For purposes of this part, principal owners are those having 20 percent or more ownership of any tourism project.

8300.3066 SECURITY REQUIREMENTS FOR TOURISM LOANS.

It is necessary for the Authority to protect its financial exposure pursuant to Minnesota Statutes, §116M.06, subd. 2. It is reasonable for the Authority to require collateral in accordance with generally accepted commercial lending practices to protect its interests in the financial assistance. The specified forms of acceptable collateral are generally accepted forms by commercial lending practices and standards. The discretion to require additional information or certificates is reasonable because it permits the Authority to enter into various types of financial assistance agreements and obtain the best available collateral as required pursuant to Minnesota Statutes, §116M.06, subd. 2, and at the same time tailor the required information to support an application to that information needed for the Authority to prudently manage the State loan programs pursuant to Minnesota Statutes, ch 116M.

8300.3067 CONTENTS OF APPLICATION FOR TOURISM LOANS.

An application for participation must be made by the financial institution on behalf of the eligible borrower on a form provided by the commissioner and must contain or be accompanied by:

A. a copy of the financial institution's file regarding the borrower's loan application;

B. a statement by the borrower, in the form provided in Minnesota Statutes, section 13.05, subdivision 4, paragraph (d), or a form similar to it if the borrower is a corporation, consenting to the dissemination of any private or nonpublic data applicable to the loan;

C. a letter containing the financial institution's assessment of the risks associated with the loan, and the credit worthiness of the borrower; and

D. a letter from the borrower demonstrating how the project meets the public purpose requirements of part 8300.3068.

8300.3067 CONTENTS OF APPLICATION FOR TOURISM LOANS.

It is reasonable to inform prospective applicants of the required contents of an application for funds under the tourism loan program. The contents of the application are reasonable and only request information necessary for the Authority to adequately evaluate the loan. Again the contents of the application are similar to the application contents for other similar Authority programs. See e.g. Minn. Rule. pt. 8300.4023. It should be noted that the application is submitted by the lender on behalf of the borrower. Thus, the application will be submitted by a lending institution. Any lending institution is familiar with various federal and state loan programs and will have experience with participation in government loan programs. Thus, the program is structured so the lending institution rather than the borrower is responsible for the submitting of an application. This should assist the tourism business by placing the responsibility with the more experienced lending institution.

8300.3068 PROCEDURES FOR TOURISM LOAN APPROVAL

Subpart 1. Preliminary eligibility review. An application is considered to have been made upon the commissioner's receipt of a completed application with all documentation and exhibits. The commissioner shall make a preliminary determination whether the application is complete and whether the borrower, project, and costs are eligible for consideration under the statutes and rules of the tourism loan program.

Subpart 2. Notification of deficiencies. If the commissioner determines the application to be incomplete, the commissioner or his or her designee shall notify the borrower, specifying the deficiencies. The financial institution has 60 days from the date of the commissioner's notification to complete the application in accordance with parts 8300.3060 to 8300.3070. If an application is not made complete within 60 days of the date of the commissioner's notification of deficiencies, the application shall be rejected for processing and the financial institution must resubmit the application at a later date in order for it to be considered by the Authority. An application which is completed by the last day of the month must be reviewed at the next month's authority meeting.

Subpart 3. Approval for processing. When an application is determined to be complete, the commissioner shall review it to assess the ability of the borrower to reasonably

repay the loan and approve or disapprove the application for processing under subpart 4.

Subpart 4. Evaluation procedures. An application which, in the judgement of the commissioner, meets the standards and requirements in the act and parts 8300.3060 to 8300.3070 shall be submitted to the Authority with a recommendation for its approval at the earliest possible time. Applications which do not meet the criteria, standards, and requirements of the act and parts 8300.3060 to 8300.3070 shall not be submitted to the Authority for its consideration until the application documents have been modified to conform to the standards of the program. If a completed application has not been modified to meet the program financial requirements within 60 days after submission, it is considered rejected and the financial institution must submit a new application for further consideration.

Subpart 5. Requirements of public purpose. Loan applications by eligible borrowers for eligible costs shall be recommended for approval by the Authority only after the commissioner has determined that the project meets one or more of the following standards of public purpose:

A. that the project would contribute to upgrading, expanding, and improving Minnesota's tourism industry;

B. that the project, in order to be competitive and bring in new travelers to the area, offer additional amenities and improve the quality of the tourism facilities in the state;

C. that the project will protect and enhance the tax base;

D. that the borrower can demonstrate a positive economic impact to the surrounding community; and

E. that the project will retain lakeshore for public use.

Subpart 6. Approval. The Authority may reject or disprove any application that does not provide sufficient documentation or otherwise comply with the provisions of the act and parts 8300.3060 to 8300.3070. If the Authority approves an application for participation, it shall pass a resolution stating the name of the borrower, a brief description of the project, the amount of participation, and the amount of and interest charged on participation.

Subpart 7. Participation agreement. After participation in a loan is approved by the Authority, the financial institution shall provide the Authority with copies of its documents for the loan. The financial institution must also submit a certificate to the Authority stating that the interest approved by the Authority will be passed on to the borrower.

8300.3068 PROCEDURES FOR TOURISM LOAN APPROVAL

Pursuant to Minn. Stat., 116J.10(h), the commissioner has the power to administer statewide programs of the Authority. It is reasonable to inform the public of the expected time frame involved in processing loan applications, of the various steps in the evaluation process itself, and of the procedures for approval and disapproval process for clarification and understanding of what is expected from an applicant, the commissioner and the Authority.

Subpart 1 discusses what is meant by a completed application to provide clarification for potential applicants. Subpart 2 provides a potential applicant procedures concerning the handling of incomplete applications. Subparts 3 and 4 describe the first review steps for completed applications based on a comparison of the project and applicant set forth in the law, general application rules and program specific rules. It is reasonable to tell potential applicants how the process works. Subpart 5 provides the reader with information concerning public purpose guidelines. Pursuant to Minnesota Statutes, § 116J.89, all financial assistance awards must fulfill a public purpose. The public purpose standards set forth in proposed subpart 5 are necessary to insure that public money is spent for a public purpose as required by the Minnesota Const. in art. X, Section 1 art. XI 2 and art. XII Section 1. Numerous Minnesota cases have set forth parameters for determining whether an expenditure of public funds is for a public purpose. The Minnesota Supreme Court has upheld the Minnesota Energy and Economic Development Act against a challenge as to the public purpose for several Authority programs. See Minn. Energy and Economic Dev. Auth. v. Printy, 351 N.W. 2d 319, 337-343 (Minn. 1984). The public purpose criteria set forth for this program are designed to insure that projects funded will improve the Minnesota tourism industry and thus, benefit an industry important to the economy of the State.

Subpart 6 provides the applicant with an overview of when the Authority either approves or disproves the application. The procedures for both approval and disapproval are described. It is reasonable to tell potential applicants what the possible outcome of the process may be. Subpart 7 discusses the documentation needed by the Authority from the financial institution after the loan is approved by the Authority. It is reasonable to tell the potential applicant what documentation the Authority will require upon approval of the participation in a loan.

8300.3069 LOAN SERVICING

The financial institution shall collect payments according to the payment schedule outlined in the note. The financial institution shall notify the Authority in case of default, as determined by the financial institution. The financial institution may retain interest collected as payment for duties performed by it pursuant to the contract in the amount of one percent per annum of the Authority's proportional share of the loan.

8300.3069 LOAN SERVICING

It is necessary for the potential lender and borrower to understand the servicing of a loan. It is reasonable for the financial institution to collect payments and notify the Authority in the case of default because the financial institution is the originator of the loan. It is also reasonable for the financial institution to retain a portion of the interest collected because of the staff time of the lender involved in the process. Such a servicing arrangement is typical of other loan participations.

8300.3070 AMORTIZATION SCHEDULES

The financial institution shall allow loan payments to be made on other than a monthly basis in order to meet the amortization schedule established by the financial institution. A nonmonthly payment schedule shall allow for seasonal payments, where income is generated, or primarily generated, because of seasonal business.

8300.3070 AMORTIZATION SCHEDULES

It is necessary for the lender and the potential borrower to be informed that the financial institution may allow other than nonmonthly loan payments. It is reasonable to provide other than monthly payments because the income generated by many of the businesses under this program will be on a seasonal basis which is typical of the tourism industry, particularly among the smaller tourism businesses.

EXHIBIT A
THE TOURISM LOAN PROGRAM

