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SMALL BUSINESS LOAN COLLECTION AND RATING POLICY

1. GENERAL STATEMENT

The Lewis County Industrial Development Agency (LCIDA) administers loan funds from the USDA and Lewis County, and other long-term notes receivables. The purpose of this policy is to set parameters around collection of loan payments and accounting of delinquent loans.

2. COLLECTION

This is the general policy information and is always subject to the Executive Director's recommendation on a loan by loan basis. It does not alter any of the terms and conditions of any loan documents.

The LCIDA will administer the following collection policy:

A. 10 to 15 days delinquent

When a loan is 10 to 15 days delinquent depending on the terms of the note a late payment notice is sent by the staff to the Borrower.

B. 30 days delinquent

When a loan is 30 days delinquent, a telephone call is made to the Borrower/Guarantor from the LCIDA staff in order to define the reason for the delinquency. The regular monthly billing is sent to the Borrower/Guarantor, which will include the two months payment due plus a late fee, as stated in the Note.

C. 60 days delinquent

When a loan is 60 days delinquent, a letter is sent to the Borrower/Guarantor from the LCIDA staff indicating the account is in default with payments 60 days past due. The letter should indicate that a meeting with the LCIDA staff is necessary to set up a schedule to correct the default, which will be presented to the Board of Directors for consideration. Further, the Borrower/Guarantor must be advised that if a repayment schedule is not adhered to, the Executive Director shall have the discretion and authority to turn the account over to the LCIDA's attorneys with instructions to begin legal proceedings to collect the full amount of the debt.

D. Foreclosure and/or Repossession

In the event of foreclosure and/or repossession, the LCIDA will advance funds necessary to protect its security interest and comply with the default rights allowed by its Security Agreement for payment of real estate taxes, insurance premiums, legal fees, disbursements…etc. These disbursements will be maintained in an asset account of the LCIDA until the result of the sale of the asset is known. In the event the costs are not recovered from the proceeds of the sale, they will be charged against the expenses of the LCIDA. In addition, if any portion of the principal balance not previously reserved against is not recovered at the time of sale, the excess will be charged as a nonrecurring expense.

If the LCIDA should become the owner of the collateral by means of the default proceedings, the reserve shall be charged against the loan balance to reduce the book value of the asset to an amount equal to the then current market value.

Based on this formula, should a specific valuation reserve be established and the borrower successfully corrects the past due status of the obligation, the LCIDA may recover the amount of the specific reserve provided.

3. SPECIFIC VALUATION RESERVE

The Executive Director shall review the status of the loan portfolio on an annual basis using the adopted Internal Loan Review/Risk Rating system. Each loan or notes receivable will be assigned a risk rating of 1, 2, 0r 3 with a corresponding reserve as follows:

1. Satisfactory 5% - The loan performs as originally agreed for six consecutive months; The board of the LCIDA is satisfied that the original problem causing delinquency has been corrected;
2. Watch 10% - The Borrower can show a profitable operation for the six-month period of satisfactory performance set forth in No. 1 above
3. Substandard 15% - Notwithstanding 1 and 2 above and in the event the collateral value is less than the loan balance, the amount in excess of the value will continue to be reserved until the loan performs for 12 consecutive months and profitability extends to 12 months

The Lewis County Industrial Development Agency's Internal Loan Review/Risk Rating Program has been established to play an integral part of the "safety and soundness" of the organization as well as being a foundation upon which its credit policies and procedures are based. It is designed to provide concise and accurate assessments of the quality of the overall loan portfolio.

The Internal Loan Review Program provides an "early warning system", a means of identifying those credits that warrant special handling and/or a greater degree of monitoring for deteriorating situations.

The loan rating definitions have been written to resemble those used by Banking Institutions and Federal and State regulators. As such, the loan rating system provides outside auditors with a method of measuring the LCIDA's asset quality and adequacy of the Allowance for Loan Losses.

In order to maintain and properly administer the Internal Loan Review/Risk Rating Program, the Executive Director and Finance Technical Specialist are required to monitor the loans administered by the LCIDA on an annual basis at 5/31 and discuss with the Loan Committee and make changes to the existing risk ratings (when appropriate), in accordance with the LCIDA Risk Rating Format.

GENERAL RISK RATING DEFINITIONS:

In assigning a risk rating, it is important to note that not all or even most of the criteria must apply in order for a loan to fall into a loan-rating category. Certain specific criteria deserve more attention than others and therefore should have a greater influence on the overall risk rating. It is often possible that a certain single criteria such as cash flow, delinquency or industry conditions could influence the upgrading or downgrading of a credit.

The loan rating definitions are as follows:

1. SATISFACTORY:

The borrower is responsible for the credit. Loans rated 1 would be included in the "Pass" category. The definition of this rating is as follows:

a. Financial statements are current, of good quality and in adequate detail.

b. Financial condition is generally on par with the industry average.

c. Earnings are generally profitable; however, occasional losses may occur. The rating would also apply to properly capitalized and liquid start- up company that has yet to establish a track record of profitable operations.

d. Cash flow has been and is expected to be sufficient to meet debt service requirements.

e. Borrower consistently adheres to repayment schedule for principal and interest.

f. Borrower generally adheres to all loan covenants, however, occasional requirements for waivers, modifications or amendments may occur but liquidity and capitalization remain acceptable.

g. Industry outlook is generally acceptable.

h. Both the integrity and the ability of management (or the individual) are good, with ability to be proven.

i. Collateral offers comfortable support and is typically somewhat better than policy guidelines. Guarantors add tangible support.

2. <u>WATCH:</u>

Assets in this category contain higher risk profiles but not to the point of justifying a classification of Substandard due to the fact that the credit is generally current and paying as agreed. Loans rated 2 would be included in the "Pass" category. The definition of this rating is as follows:

a. The financial statements may be missing, seriously outdated, of poor quality, or lacking in important details. If this is the case, the officer must investigate whether the non-receipt of financial statements on a timely basis is a meaningful red flag indicating the borrower is in trouble. If the statements have not been received six months after date of fiscal year end, the officer must prepare a brief file entry justifying the continuation of the existing rating, if appropriate based on other sources of knowledge of the credit or initiating a downgrade to whatever rating the officer believes is warranted based on their findings.

b. Financial condition is below the industry average and/or needs improvement.

c. The borrower is experiencing negative trends and/or erratic or unstable financial performance relative to industry norms. The borrower may have suffered a substantial loss in a recent period or moderate losses over a period of more than 18-months; however, losses have not been to the degree to have adversely affected the balance sheet.

d. Cash flow has generally been adequate but, if existing trends continue, may be potentially inadequate to meet projected debt service requirements. On an exception basis, the officer may consider a Watch (rather than lower) rating based upon an adequate secondary source of cash flow. Reliance on a secondary source can be used to justify a Watch rating only when that source is liquid, when its continuing availability has been verified, and when the LCIDA has legal rights to it.

e. Borrower generally adheres to repayment schedule for principal and consistently for interest. On an exception basis, a loan with delinquent payment(s) and/or maturity date missed may continue to qualify for a Watch rating if a well-defined plan to bring the payment(s) current within a reasonable timeframe. If the plan calls for a takeout or payoff of the loan, the source of repayment must be a reliable one.

f. Borrower may have violated one or more financial or other covenants, liquidity and/or capitalization may need improvement.
g. Industry outlook may be unfavorable.

h. The integrity of management (or individual) remains good.

i. Collateral offers moderate coverage and is typically at policy limits. There is perhaps some reliance on soft assets. Guarantors add nominal financial support.

j. Borrower closes business but making loan payments.

3. <u>SUBSTANDARD:</u>

A substandard asset is inadequately protected by the current sound worth and paying capacity of the borrower or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the LCIDA will sustain some losses if the deficiencies are not corrected.

A general rule of thumb is that a relationship that previously required the normal degree of monitoring begins to absorb an inordinate amount of the officer's time for servicing and/or to incur an increasing amount of carrying costs. The existence of any of the following conditions warrants consideration for a substandard rating:

a. The financial statements may be missing, seriously outdated, of poor quality, or lacking in important details. If this is the case, and there are other reasons to believe that the financial condition of the borrower has deteriorated, then the loan officer should strongly consider classifying the relationship Substandard.

b. Financial condition is less than satisfactory.

c. The borrower is experiencing negative trends and losses.

d. The primary source of repayment is inadequate to meet current debt service requirements, and, unless present conditions improve, it is potentially inadequate to meet projected debt service requirements. The borrower may have reached the point of employing its secondary source of cash flow. Although the secondary source may be difficult to quantify, it must appear supportive based on reasonable analysis and be generally marketable under normal conditions.

e. Borrower inconsistently adheres to repayment schedule for principal and interest. The Substandard rating may also apply when interest is current but principal is delinquent and a defined plan to resolve the situation within a reasonable timeframe has not yet been established.

f. Borrower may have violated one or more financial or other covenants, resulting in unsatisfactory liquidity and/or capitalization.

g. Industry outlook may be unfavorable.

h. Either the integrity or the ability of management may be in question.

i. Collateral may not provide sufficient protection. Guarantors add minimal financial support.

j. Borrower closes business