

CLEAN ENERGY FINANCE GUIDE, THIRD EDITION

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Chapter 13.

Small Business Financing Options for Clean Energy Projects

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A. Introduction

Small business owners rarely have much time to spend to arrange financing unless they see a large direct benefit to their company. In an expanding economy they are inclined to invest in projects that increase sales, while in tight economies they focus on reducing expenses, saving money, and surviving. Spending money to save money can be a difficult argument to make to a small business owner, especially in a down economy. Yet lessons learned from the successful experiences of small businesses since the mid-1990s show that energy efficiency and renewable energy projects demonstrate time and again their capacity to improve the cash flow of a small business.¹

According to the ENERGY STAR[®] program, 30% of the average utility bill pays for wasted and/or underutilized energy. Financing energy efficiency projects is a way to capture the value of the waste by monetizing current and future energy savings that come from installing energy efficiency (EE) and renewable energy (RE) improvements.

Small businesses, however, generally find it difficult to obtain financing for their clean energy projects; and when they do, they often feel that the rates are high and the repayment terms short. Funds provided by the American Recovery and Reinvestment Act of 2009 (ARRA) can be used to support small business financing programs by providing low-cost capital to revolving loan funds for direct lending and/or credit enhancements to existing lenders to help reduce program risk. That should result in improved loan pricing and longer terms to the borrower for clean energy projects. However, ARRA funds come with certain strings attached,² which can affect a project's cost and small business' willingness to engage in the financing.

This chapter of the Clean Energy Finance Guide reviews traditional financing options available to small businesses for clean energy projects outside of ARRA, and the ways grantees can use ARRA funds to facilitate loans for EE/RE projects in the small business sector.

B. Elements of a Successful Small Business Financing Program

Successful clean energy financing programs have many common elements: a simple application process, fast credit decisions, reasonable pricing, and fast loan closings with documents that are written in plain, easy to understand language. In general, small businesses use the interest rate as a litmus test to confirm that they have a "good deal." So a grantee's loan program rate should be at least as good as, and preferably better than, what the small business could get on its own. The small business owners' perception that they can get a better deal somewhere else will slow the decision process and may result in the clean energy project never being implemented because the owners get pulled back into the daily needs of running their small businesses.

¹ http://www.energystar.gov/index.cfm?c=sb_success.sb_successstories_state

² Davis-Bacon (prevailing wages) and National Environmental Protection Act (NEPA) compliance requirements can have the effect of increasing clean energy project costs.

Successful programs like Connecticut’s Small Industrial and Commercial Loan Program, Massachusetts’ MassSaves, and Sacramento Municipal Utility District’s Commercial Energy Efficiency Loan Program directly incorporate trade allies into the sales process. Those allies are the companies that sell and install solar panels, wind projects, and energy-efficient insulation, windows, roofing, hot water heaters, lighting, appliances, and heating, ventilation, and air-conditioning equipment. (Many of those firms may be small businesses themselves.) From experience, the trade ally companies know that customers don’t usually buy products or agree to do efficiency projects just because of low- or zero-interest rate programs. Rather, attractive financing facilitates the sale of EE and RE projects only after the buyer has acknowledged the benefits of the projects. Trained vendor salespeople have proven to be extremely important in communicating the benefits of clean energy projects to small businesses and then using financing to “close the sale.”

The financing process itself is critical to a program’s success. One sure way to lose the support of the trade ally network is to delay the payment of their invoices. When setting up a financing program for small businesses, whether it is a proprietary revolving loan fund or working with third- party lenders, grantees are advised to involve trade allies in the program marketing and outreach activities.

C. Defining Small Business

Small businesses face a number of challenges and options when financing EE/RE projects, some of which stem from how different entities involved in the financing process define “small business.” Interestingly, “small business” is defined differently by different organizations. Below are four different definitions for small business, one each from the U.S. Small Business Administration, electric and gas utilities, financial institutions, and a study sponsored by the Equipment Leasing & Finance Foundation.

The U.S. Small Business Administration (SBA) uses the number of employees and/or the annual receipts as key measurements. SBA evaluates industries independently and publishes “size standards” guidelines for each. The most common categories are 500 or fewer employees for manufacturing industries, 100 or fewer for wholesale trade, \$7 million in annual sales for most retail and service organizations, and \$0.5 million in revenue for agricultural industries. The size list is organized by NAICS codes (The North American Industry Classification System) and is available on the SBA web site.³

Electric and gas utilities measure small businesses by the amount of energy they consume. For example, some electric utilities consider a small business one that has a peak demand of less than 100 kW per month. Other utilities define small business differently when qualifying them for energy efficiency incentives. For example, NStar in Massachusetts defines a small business as one with a peak demand of 10 kW per month or less. Peoples Gas in Illinois defines a small business as customers that consume less than 41,000 therms per year.

In addition to the size of the business, financial institutions categorize by the size of the loan. While the exact break points may differ by lender, in general, loans under \$25,000 are considered “micro loans,” from \$25,000–\$250,000 “small ticket,” from \$250,000–\$5 million “middle market,” and over \$5 million “large ticket.” The pricing models and underwriting procedures for each of those categories differ, even within the same lending institution.

In 2008, The Equipment Leasing & Finance Foundation commissioned Global Insight to study how small businesses purchased and paid for equipment. In that study the “small businesses” were defined as

³ <http://www.sba.gov/size/sizetable2002.pdf>

businesses with fewer than 100 employees; those having fewer than 50 employees were considered “very small.” That characterization is probably more closely aligned with the way most people interpret “small.” The study found that very small businesses only finance about 17% of their capital purchases; the majority of them paid cash or put it on their line of credit at their bank. Small businesses (those with 50 to 99 employees), however, financed almost 45% of their capital purchases. The difference between the two percentages may reflect the difficulty that very small businesses have when trying to borrow money.

D. Big is Better ... But Not Always

The legal structure of a small business may also play a role in determining the terms and conditions of a project’s financing. The following are examples of common legal structures:

- **Sole proprietorship** is a type of business entity in which there is no legal distinction between the owner and the business. Profits (and losses) go directly to the owner(s) and are reported on his/her personal income tax returns. In a sole proprietorship, the owner’s credit history is one of the primary considerations for a loan approval along with time in business, prior loan history, and trade references.
- **A general partnership** in civil law refers to the participation of two or more individuals in a common business activity. Individuals are personally liable (jointly and individually) for the obligations of the general partnership. As such, all partners’ personal credit histories are primary considerations for loan approvals along with time in business, prior loan history, and trade references.
- **Corporations** are considered natural persons under the law and can enter into their own contracts (including loans). A corporation’s legal exposure is limited to its balance sheet, which excludes the owner’s personal assets. There are different kinds of corporations:
 - A “**C corporation**” is taxed as a stand-alone entity, meaning earnings may be subject to “double taxation” (once at the corporate level and again as dividends to the owners). C corporations may be able to obtain credit without the owner’s personal guarantee if the corporation has done so in the past for a similar or larger lending amount and can show profitability and a strong balance sheet. However, most small business C corporations are required to give the personal guarantee of the owners to obtain financing, especially when the owner is needed to run the business.
 - A “**Sub-chapter S corporation**” is not considered a tax-paying entity and passes all profits (and losses) on to the owners. This type of corporation fits somewhere between sole proprietorships and C corporations when it comes to the need for the owner’s personal guarantee on loans.
- In general, small businesses that are commercial properties or projects involving real estate are organized as either **Limited Partnerships**⁴ (LPs) (wherein financial exposure (liability) is limited to the assets of the Limited Partnership and the general partner, but not to the limited partners) or **Limited Liability Companies** (LLCs) (a blend of partnership and corporate benefits by limiting liability to the balance sheet and passing tax obligations to the owners). Upon credit evaluation, many LPs and LLCs have balance sheets that reflect small equity positions in the company. These firms frequently operate at a tax loss, and positive cash flows realized from operations are often distributed to the owners. Financial institutions usually

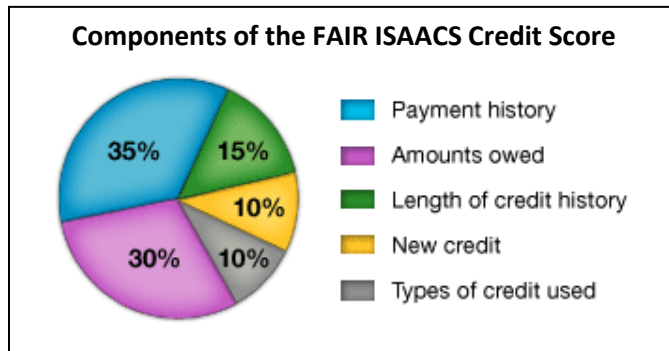
⁴ There are two kinds of partners in a Limited Partnership: General and Limited. The General Partner is the managing partner. Typically the General Partner is a corporation, which, in turn, provides individual owners with legal protection against creditors.

request personal guarantees on loans to LPs and LLCs, especially when the balance sheet is not strong.

Even when a small business is legally considered a separate entity from its owners, with separate liabilities and assets, the personal guarantees of the owners of small businesses are usually required to obtain credit from traditional lenders (e.g., a bank, leasing company, or commercial lender) unless the business has been established under the same ownership for many years (10+), has a strong balance sheet, predictable positive cash flow, and professional management in place.

In summary, smaller businesses often find it more difficult to obtain loans than larger businesses. When they can obtain financing, it is often at a higher interest rate with shorter terms and requires additional collateral and guarantees. In general, owners must demonstrate a personal net worth in excess of the amount being borrowed, and they must support the borrowing via personal guarantees. Some commercial lenders will fund up to \$100,000 for any kind of project simply based on the personal credit report and FICO score of the owners.

E. How Is Credit Risk Determined for a Small Business?



As stated above, it is usually the personal credit record of the small business owners that makes or breaks the deal with a lender. Fair Isaacs Corporation, a publicly traded company, created a scoring model that has become the industry standard for evaluating consumer credit. This score, called the FICO® Credit Score, is based on proprietary formulas that include a composite analysis of an individual's payment history, amounts owed, length of credit history, new credit, and types

of credit used. A score of 720–850 is the highest (best) category, while 500–559 is the lowest. Today, a score of 640 appears to be a common cut-off point for many commercial lenders. The underlying specifics of FICO Credit Score formulas are as secret as the recipe for Coca Cola®. The credit score's impact on a loan transaction's interest rate is substantial, with the lowest score costing double or more than the best score.

According to the Fair Isaac Corporation, owner of the FICO brand,

"FICO Scores are calculated from a lot of different credit data in [your] credit report. This data can be grouped into five categories [as shown in the chart above]. The percentages in the chart reflect how important each of the categories is in determining your FICO score. Those percentages are based on the importance of the five categories for the general population. For particular groups—for example, people who have not been using credit long—the importance of these categories may be somewhat different."⁵

The three primary business or commercial bureau credit repositories in the United States are Dun & Bradstreet (D&B), Experian Business, and Equifax Small Business Financial Exchange (SBFE). D&B is the oldest and most commonly used credit service for business; the D&B rating system appears in the chart below.

⁵ <http://www.myfico.com>

The D&B Financial Strength rating is based on the net worth or issued capital of the company. The D&B Composite Credit Appraisal is important to lenders as it provides insight into the risk of lending to (or

FINANCIAL STRENGTH (Net Worth)		COMPOSIT CREDIT APPRAISAL				
Rating	US\$	High	Good	Fair	Ltd.	No Info
5A	60,000,000 and over	1	2	3	4	5
4A	25,000,000 to 59,999,999	1	2	3	4	5
3A	12,000,000 to 24,999,999	1	2	3	4	5
2A	2,500,000 to 11,999,999	1	2	3	4	5
1A	1,200,000 to 2,499,999	1	2	3	4	5
A	600,000 to 1,199,999	1	2	3	4	5
B	345,000 to 599,999	1	2	3	4	5
C	175,000 to 344,999	1	2	3	4	5
D	120,000 to 174,999	1	2	3	4	5
E	60,000 to 119,999	1	2	3	4	5
F	35,000 to 49,999	1	2	3	4	5
G	15,000 to 34,999	1	2	3	4	5
H	0 to 14,999	1	2	3	4	5

Source: <http://www.dnb.com.lv/en/rating.html>

the financial condition of) the company. A company rated “1” is considered minimal risk; “2” is low risk; “3” is greater than average risk; “4” represents significant risk; and “5” means there is insufficient information available to assign a risk category. In addition, D&B uses a model called Paydex[®] that tracks a company’s payment history with its vendors. A Paydex score of 80 means that the customer pays promptly. Less than 80 means that the customer pays beyond the terms (slow), and more than 80 indicates that the customer anticipates payments (e.g., takes discounts on invoices).

Experian Business Reports uses a similar system, called a Credit Ranking Score, to predict payment behavior. Customers are rated between 0 (high risk) and 100 (low risk). Equifax offers a Small Business Credit Risk Score, designed for use by the financial services industry. It uses a numeric score between 101 and 992, with a lower score indicating higher risk for serious delinquency.

F. Financing Options for Small Businesses

When designing a finance program, grantees should bear in mind that from the small business borrower’s perspective, obtaining financing is a two step process: (1) choosing the underlying financing structure (e.g., loan or lease), and (2) deciding upon the source of capital to be used. Often the source of capital will determine the type of financing structure used. For example, a borrower may wish to expense the financing payment for tax purposes, which implies entering into an equipment lease and working with a leasing company (see Section titled *Equipment Leasing* below). Banks, in turn, generally prefer to issue loans. Because the grantee becomes the source of capital, the grantee has control over the choice of financial structure to be used.

Different types of financing structures may have distinct tax and financial reporting consequences for the borrower. For example, small business borrowers often want “off balance sheet” treatment for their energy efficiency projects. “Off balance sheet” treatment means that the energy project and financing do not appear on the balance sheet as an asset or liability, and the small business owner can deduct the entire financing payment as a business expense. This deduction reduces the business’ profit and, consequently, its tax liability (which is based on net profits).

Borrowers with restrictive covenants⁶ in place with their current lenders may find that adding debt to the balance sheet changes their financial ratios. Different financial ratios can result in higher interest rates on existing loans, can limit borrowing capacity, and can even prompt a lender to call in existing loans. That is why for certain borrowers, keeping the asset off the balance sheet is important. However, for an asset to pass the economic test needed to obtain off balance sheet treatment, it must retain its value over the term of the financing. With few exceptions, energy efficiency equipment or retrofit products do not have much resale value and do not qualify for off balance sheet treatment. Imagine trying to repossess and resell insulation added to a building's roof or walls, or removing and remarketing a recently installed lighting system.

The alternative is to show the asset (e.g., the clean energy project) and corresponding liability (loan) on the balance sheet, and depreciate the asset over its useful life (the period set by the IRS during which the asset is expected to be used).

The remainder of this section describes the range of financing structures and sources of funds open to a typical small business.

- **Commercial Loans** are commonly used to finance energy projects. They may be unsecured (known as “signature loans,” “good faith loans,” or “character loans”) or secured by certain assets of the business or owner(s).⁷ Typically, secured loans reflect the reduced risk to the lender by having lower interest rates. Traditional lenders will look at business history, company assets, and cash flow to decide whether or not to approve a loan. Newer or financially challenged businesses may not qualify for a loan without providing substantial tangible collateral. For example, many banks require compensating balances to be held in their institutions, place restrictive covenants on the operations of the business until the loan is paid in full, and will not lend 100% of the cost of the asset (the clean energy project). Large, national banks tend to look for larger clients and loans, while local community banks are often more flexible when it comes to loans for small businesses. Some credit unions also offer business loans to small businesses.
- **Equipment Leasing** is often referred to as “creative financing” because leases can be structured to address the particular tax strategies and cash flow needs of the lessee (borrower). For financial reporting purposes, leases fall into one of two categories: **capital** or **operating**. Capital leases are reflected on the lessee's (borrower's) balance sheet, while operating leases are considered “off balance sheet” financings.⁸ More information on operating leases is available in the Financial Accounting Standards Summary of Statement No. 13 (FAS 13) at www.fasb.org/summary/stsum13.shtml.
- **A Tax or True Lease** is a lease with a true “fair market value” purchase option, essentially a long-term rental agreement. It may be reflected on the balance sheet for financial reporting purposes, yet it may qualify as an expense item for tax reporting purposes.

In addition to tax considerations, most leases can be structured with uneven payments that reflect the timing of energy savings of the installed equipment. Also, unlike most

⁶ Restrictive covenants are clauses in the lending document that impose restrictions on the borrower by the lender. Commonly found in bank loans, they may include keeping minimum balances on deposit with the lender, defining minimum working capital requirements, maintaining certain financial ratios, limiting the sale of assets, etc.

⁷ This differs from a secured loan in the residential market, which implies taking a security interest in the real estate of the borrower.

⁸ At the time of this writing, the current classification is being reevaluated by the Financial Accounting Standards Board (FASB). The expected outcome is that operating leases will be included on balance sheets.

bank/traditional loans, leasing can provide 100% financing. When dealing with clean energy projects that offer state or federal tax credits (which can only be used by taxpaying, profitable organizations), operating or true leases may be a way to separate ownership from the use of the equipment. In this way, the value of the tax credits may be reflected in lower lease pricing to the user.

- **Equipment Sales Agreements** are financing contracts in which the seller keeps the title of the equipment and the right of repossession (should the buyer default) until the buyer finishes paying for it. From an accounting perspective, the buyer treats the asset as if he/she owned it, depreciating the asset and expensing interest payments.

Many large equipment vendors offer financing programs to help promote the sale of their equipment. That is often handled through captive financing companies (a finance company generally owned by a manufacturer and occasionally a large distributor) at attractive rates.⁹ The financing structures they commonly use are **equipment sales agreements**, **lease financing**, and for large projects **power purchase agreements**, **energy service agreements**, and **performance contracts** (see Chapter 12 for information on the financing of large commercial projects).

Less Attractive Alternatives for Clean Energy Financing

Some businesses have a **line of credit** established with their banks. That is best used for short-term working capital needs like inventory purchases, and is not recommended for the purchase of longer term assets such as energy efficiency and renewable energy projects. Small business owners might decide to take out a **home equity loan** to obtain the funds needed for a clean energy project. While the interest rates and terms will be attractive, putting one's home at risk will not appeal to many small business owners. **Credit cards** are another option; however, they tend to be expensive sources of long-term capital and are not recommended for clean energy projects.

G. SBA Loan Guarantees

The U.S. Small Business Administration (SBA) offers loan guarantees to banks, savings and loan associations, credit unions, community development financial institutions, and other authorized specialty lenders. While SBA does not lend money directly to small businesses (other than for disaster relief loans), it can guarantee certain portions of business loans made by banks and other lenders for loans that conform to SBA guidelines.

Personal guarantees from the owner(s) of the small business are always requested on SBA loans, and contrary to popular belief, SBA loans are not made to persons or businesses with bad credit. To qualify for an SBA guarantee, the business must show that it cannot obtain financing at reasonable rates and terms without such a guarantee, and that it has the cash flow needed to service the loan.

The most common SBA loans are described below:

- **SBA's 7(a) Loan Program** is its most popular and flexible program. It can be used for any type of asset (including energy efficiency improvements). It includes several different **Express Programs** that offer "streamlined and expedited loan procedures for particular groups of borrowers,"¹⁰ businesses in Historically Underutilized Business Zones (HUBZones), and veteran-

⁹ Captive finance companies may have the advantage of offsetting some of their financing costs by using the profit margin in the sale of the item, resulting in lower rates.

¹⁰ www.sba.gov/financialassistance/borrowers/guaranteed/7alp/FINANCIAL_GLP_7ALP_EXPRESS.html

owned businesses. **The Small/Rural Lender Advantage Program** helps small community/rural-based lenders “promote the economic development of local communities, particularly those facing the challenges of population loss, economic dislocation, and high unemployment.”¹¹ **Pollution Control Loans** “are 7(a) loans specifically designated for pollution control. The program provides financing to eligible small businesses for the planning, design, or installation of a pollution control facility. This facility must prevent, reduce, abate, or control any form of pollution, including recycling.”¹²

- **SBA’s CDC/504 Loan Program** is a long-term financing tool for economic development within a community, providing long-term fixed-rate financing. It can be used for the “construction of new facilities or modernizing, renovating or converting existing facilities,”¹³ which includes energy efficiency improvements. However, CDC/504 loan programs may require some structuring because to qualify one must have 50% of the funds coming from a senior lender, 40% from a junior lender (e.g., a Community Development Corporation), and 10% from the borrower.
- **SBA’s Micro Lending Program** provides small businesses with small short-term loans for under \$50,000. Micro loans can only be used for working capital and acquisition of materials, supplies, furniture, fixtures, and equipment, which may include clean energy equipment.
- **The 8(a) Business Development Program** assists in the development of small businesses owned and operated by socially and economically disadvantaged individuals, such as women, minorities, veterans, and disabled persons.

SBA loan terms and conditions vary greatly by program. For example, SBAExpress can cover up to \$350,000 with terms up to 7 years at interest rates indexed to Prime Rate, LIBOR, or the optional peg rate (published quarterly in the Federal Register). PatriotExpress, on the other hand, will finance up to \$500,000. For details about individual loan programs, see the U.S. Small Business Administration’s website at www.sba.gov.

Because the SBA guarantees can be as high as 90% of a loan, additional credit enhancements that ARRA grantees might offer may not be particularly interesting to a third-party lending institution. Offering a lender an additional 10% or even 20% loan loss reserve on an SBA loan that is already guaranteed at 90% may not be attractive enough to entice lending partners to participate in ARRA-funded clean energy loan programs. However, some commercial lenders may find the marketing support behind an ARRA-funded EE/RE loan program appealing because it helps bring more clients to their financial institution. In addition, SBA program guarantees are paperwork intensive for the lender. Some lenders may find an ARRA-funded loan loss reserve-based financing program attractive if it requires minimal paperwork.

H. Working with Community Development Financial Institutions

Other financing sources for small businesses include Community Development Corporations (CDCs) and Community Development Financial Institutions (CDFIs). Many of these entities operate revolving loans funds, which they will consider using to make loans for energy efficiency and renewable energy building improvements. According to the CDFI Coalition of Community Development Financial Institutions, there are more than 850 CDFIs in the United States. CDFIs “serve economically distressed communities by providing credit, capital, and financial services that are often unavailable from mainstream financial

¹¹ www.sba.gov/financialassistance/borrowers/guaranteed/7alp/FINANCIAL_GLP_7ALP_RURAL_LEND.html

¹² www.sba.gov/financialassistance/borrowers/guaranteed/7alp/POLLUTION_CNTRL_7A-LOAN-PROG.html

¹³ www.sba.gov/financialassistance/borrowers/guaranteed/CDC504lp/index.html

institutions. CDFIs have loaned and invested over billions [of dollars] in our nation’s most distressed communities.” (Source: CDFI Coalition website <http://cdfi.org>).

The tables in Attachments A and B present a detailed comparison of six types of CDFIs. The first table evaluates the CDFIs by purpose, start-up considerations, governance and ownership, and regulation. The second table continues the comparison with the categories of borrowers, capital sources, financial products and services offered, and technical assistance provided. These charts are taken directly from the CDFI Coalition website <http://cdfi.org>.

CDFIs have experience in originating, underwriting, and/or servicing loans. As such, they could serve as partners to help manage and administer ARRA grant funds when establishing a revolving loan fund. In addition, they may be able to help leverage ARRA funds through participation agreements with other sources of capital with which they have existing relationships, supported by loan loss reserves and interest rate buydowns.

H. Use of ARRA Funds in Small Business Lending

The Recovery Act has earmarked about \$1 billion to be used to promote financing of energy efficiency and renewable energy projects, mostly for residential programs and in a few cases for small commercial programs.¹⁴ At the time of this writing, many of those programs are still under development. ARRA funds can be used to facilitate small business efficiency improvements in a number of ways as described below.

Direct Loans

ARRA funds can serve as capital for loans made directly to small businesses. If the grantee wishes to manage its own fund, it must first decide whether or not it has the skill set, staffing, and software needed for originating loan applications, credit underwriting, document preparation, and loan servicing. Many of those services can, in fact, be outsourced to specialty organizations, CDFIs, other revolving loan funds, nonprofit organizations, or commercial lenders. The leverage on such direct lending is limited to how quickly the loans mature. As one example, Colorado is using State Energy Program (SEP) funds to provide loans to clean energy companies (small businesses), originated through the Colorado Housing Finance Authority (CHFA).

Direct Loan Capital Supplemented by Private Capital Commitments

Some grant recipients are able to entice other lenders to participate in a revolving loan fund. For example, Phoenix, Arizona, is developing a program that will mobilize \$4 million of ARRA funds to seed a pool of funds to which other capital providers would add their own loan capital to assist small businesses in implementing clean energy projects. Other grantees are trying to set up financing for small businesses that would have participation agreements with large national banks, which, in turn, would receive Community Redevelopment Act (CRA) credit because of the dire economic situations in the grantees’ locales. In such cases, ARRA funds would be used for direct loans, interest rate buydowns, and loan loss reserves.

¹⁴ It is important to note that commercial and industrial contracts over \$2,000 are subject to the National Environmental Policy Act (NEPA) requirements and the Davis-Bacon Act (DBA), meaning prevailing wages must be paid on the project. In the few states where the prevailing wage is already similar to the existing wage, Davis-Bacon may not be an obstacle. However, DBA and NEPA are potential pricing challenges that exist for commercial and industrial projects that do not exist in the residential market. For more information on the Davis-Bacon Act, visit www1.eere.energy.gov/eere_faq/default.aspx?pid=10&spid=1.

Credit Enhancements

Another way for grantees to increase the leverage of other funds is by providing credit enhancements to attract third-party capital (see Chapter 1, Section E). Such credit enhancements can come in the form of interest rate buydowns and loan loss reserves. Note that working with traditional third-party lenders (banks, credit unions, etc.) may be a way to quickly jump-start a clean energy loan program. Most lenders will not be excited about creating a new financing program or loan product unless they feel that substantial volume can be generated as a result of the program. They will, however, be interested in the marketing support the grantee will be providing to the program, as lenders are always looking for ways to find new customers. Banks, for example, welcome new customers because they see them as an opportunity to cross-sell other financial products (i.e., payroll and retirement accounts, Christmas or vacation savings clubs, etc.). Another example, also from Colorado, is a new program through which the CHFA offers a loan loss reserve to participating financial institutions that make loans to support qualifying clean energy projects.

Preliminary Energy Efficiency Audits and Technical Assistance

ARRA funds may also be used to pay for preliminary energy efficiency audits. When appropriate, and if the project is large enough, it may be possible to include the cost of those audits as part of the project cost when financing, thereby allowing the grantee to recover and recycle funds for that service.

Marketing and Administrative Expenses

ARRA funds may be used for administrative expenses (subject to a cap of 10% of the total Energy Efficiency and Conservation Block Grant or SEP grant), marketing costs, hiring a third-party administrator, and other related administrative costs.

Examples of Small Business Loan Programs

A number of small business clean energy loan programs are currently up and running, and more are under development. See Attachment C for examples of existing programs.

Attachments

- A. CDFI Types by Purpose, Start-up Considerations, Governance & Ownership, and Regulations
- B. CDFI Types by Borrowers, Capital Sources, Financial Products & Services Offered, and Technical Assistance Provided
- C. Examples of Small Business Loan Funds