



# Local Business C2B Program



May 2020

## SUMMARY OF TERMS

**Purpose:**

COVID-19 has severely impacted local businesses throughout the United States. Local businesses, most of which have fewer than 100 employees, employ over 50% of the U.S. workforce. Without further assistance, 52% of local businesses will fail in the next six months, *Bloomberg News* reports. Preventing these business failures is critical to the stability of the US economy and local communities.

Government support programs, such as the Paycheck Protection Program, have been effective in providing short-term support for these businesses, but once the United States reopens, more funding will be needed. Given the risk of failure, bank loans will be hard to obtain. Equity investment is needed, but local businesses do not have easy access to traditional equity capital. Their capital needs are too small to be interesting to most institutional investors, and even if there were interest from these investors, the record keeping and financial modeling capabilities of most local businesses may not be sufficiently robust to address the demands of institutional investors.

Peer-to-peer investment is the solution to this problem, just as it has been in the consumer finance sector. For the past decade peer-to-peer lending platforms have filled the consumer credit void created by the withdrawal of traditional banks from consumer lending. Entities like Prosper and Lending Club connect borrowers with individuals who provide funds for loans. Together, Prosper and Lending Club have drastically expanded access to credit for many consumers who lack access to traditional funding sources for personal loans.

The C2B Program combines peer-to-peer lending with crowdfunding and enables local businesses to access capital funding available from residents of their communities who already know the business, appreciate its value to the community and are willing to support it by more than mere patronage. For investors, the program allows members of the community to invest in their communities and achieve both social and investment returns. Investors will be able to direct capital to a particular business

participating in the program, or to categories of local businesses in a particular community, such as restaurants in Falls Church, Virginia.

We have named our program the C2B Program to capture the local nature of the initiative. The “C” stands for customers or the community that is supporting their favored local businesses. This local flavor adds a community-based twist to peer-to-peer lending or crowdfunding by providing financial support by the individuals who previously procured or consumed the products or services of the local business and who want to do more to help ensure the well-being of the local business.

The program disintermediates capital formation by using already established peer-to-peer lending models in order to deploy small amounts of capital efficiently where it is needed the most, very similar to a ride-sharing service such as Uber or Lyft, which matches riders and drivers.

Government support under this program will be available for investment in some local businesses, sectors of local businesses and communities that most need support and that often represent the highest risk for the investor. The types of projects that may benefit from government support under this program can change over time depending on imbalances between capital needs and available capital.

**Program:** The C2B Program.

**Sponsor:** The Program will be sponsored by the Small Business Administration, another agency of the federal government designated by the United States Treasury, or even a state or local government if the Program is not implemented nationwide. The applicable government entity may delegate administrative authority to non-governmental entities, such as community development financial institutions or experienced non-profits working in community development.

**Program Criteria:** The rules and regulations of the Program will be established by the Sponsor of the Program and set forth in the Program Guide, which will be publicly available on the Program website.

**Eligible Local Business:** An Eligible Local Business under the Program is any local business in operation before the impact of COVID-19 that satisfies the Program Criteria for Program participation, including:

- Majority-owned by the persons operating the business.
- At least five (5) employees but no more than one-hundred (100) employees.
- The amount of total income, total taxable income and total tax or equivalent line items, as reported on the business’ federal tax forms for the most recently completed year, certified by the

business' chief executive officer or equivalent, and financial statements of the issuer certified by the same officer. If financial statements of the issuer are available that have either been reviewed or audited by a public accountant, then, those financial statements can be provided instead of the other financial information.

- Credit report for the business owner (if sole proprietorship or single-member LLC) and credit report for the business.
- Schedule of debt obligations.
- At least \$300,000 in annual revenue for the past two (2) years.

**Peer Contributor:** Subject to certain individual investment limits, as required to comply with applicable securities laws, a natural person who satisfies the criteria to be a Peer Contributor established by the Program Criteria. Institutional investors will not be Peer Contributors.

**C2B Platform:** The lending platform established and managed by the Sponsor to:

- Process applications from Eligible Local Businesses and Peer Contributors seeking to participate in the Program.
- Process the funding of Notes issued by Eligible Local Businesses to Peer Contributors.
- Act as agent for Notes issued by Eligible Local Businesses and funded by Peer Contributors.
- Manage reporting from Eligible Local Businesses to Peer Contributors and the Sponsor.
- Facilitate transfers of Notes to other Peer Contributors.
- Process the conversion of Notes to profit interests in the Peer Contributors.
- Process the redemption of Notes by the Eligible Local Businesses.
- Process the assignment of Notes to the Sponsor under the Program Support.

**Program Criteria:** The rules and regulations of the Program to be established by the Sponsor of the Program and set forth in the Program Guide, which will be publicly available on the Program website.

**Application Process:** To be set up for funding under the Program, the Eligible Local Business must submit to the Sponsor the documents required by the Program Guide, including the following:

- A completed, signed and dated application form.
- The financial information and credit reports identified above.
- Quarterly P&L information for the four (4) most recent quarters ended prior to the date of application, if available.

- A Business Plan, in the form specified by the Program Guide.

**Note:** An unsecured interest-bearing Note issued by an Eligible Local Business to the C2B Platform as agent for a Peer Contributor, the terms of which will be established by the Program Criteria.

The Peer Contributor will have the right at various times during the term of the Note to convert pursuant to a schedule attached to the Note a portion of the outstanding principal amount of the Note, and any unpaid but accrued interest thereon, into a profits interest in the profits of the Eligible Local Business. To the extent that the Peer Contributor exercises its option to convert a portion of principal due into a profits interest, its right to Program Support will be terminated. For example, a \$5,000 Note would give the Peer Contributor the option on each annual anniversary of the issuance date of the Note to convert the note into a Fixed Percentage profits interest in the profits of the Eligible Local Business, calculated in accordance with the terms of the Note. The Peer Contributor will hold the profits interest until such time as the maximum payment due to it has been satisfied from the profits of the Eligible Local Business.

The investment will exit the C2B Platform when the Note is converted to a profits interest in the Eligible Local Business, and the Peer Contributor will surrender any claims to Program Support.

If the Peer Contributor does not exercise its conversion right, all amounts owed under the Note will be due on the final maturity date. The final maturity date may be accelerated automatically upon the occurrence of certain events of default under the Note as discussed below. If the Note is not repaid in full on the final maturity date and if Program Support applies, then the Peer Contributor may instruct the C2B Platform as agent to assign the Note to the Sponsor and recover a portion of its investment under the Program Support.

**Investment Amount:** The maximum amount of the Note will be sized based on the Program Criteria, but in no event will exceed \$100,000 in principal amount.

**Fixed Percentage:** The fixed percentage of profits interest that the Eligible Local Business will issue to the Peer Contributor upon the Peer Contributor's election to exercise its conversion right under the Note. The fixed percentage will be established by the Sponsor and the Eligible Local Business at the time the Note is issued based on the Sponsor's assessment of the Eligible Local Business (based on a review of the financial statements and business plan). The profits interest is intended to allow the Peer Contributor the right to receive an amount from future profit of the Eligible Local Business up to the full repayment of the Note, plus a supplemental payment or "upside reward" in excess of that amount. The right to the

profits interest will be extinguished once the specified amount has been recouped.

**Ranking:** The Note will be an unsecured debt obligation of the Eligible Local Business. It will rank as subordinate to secured creditors of the Eligible Local Business and *pari passu* with other unsecured obligations of the Eligible Local Business.

**Maturity:** The final maturity of the Note will be five (5) years from the date of issuance, subject to any earlier conversion or to acceleration upon the occurrence of any event of default discussed below. No principal will be due and payable on the Note prior to the maturity date.

**Interest Rate:** The principal of the Note will accrue interest at a rate of 4% per annum until the third anniversary of the Note, and after the third anniversary of the Note until the maturity of the Note, the principal will accrue interest at a rate of 2% per annum. Interest shall be payable quarterly in arrears on January 1, April 1, July 1, and October 1 of each year.

**Redemption:** The Note may be redeemed by the Eligible Local Business at any time beginning on the first anniversary of the issuance date if the Peer Contributor does not elect to exercise its conversion right. If the Note is redeemed at any time after the first and before the second conversion date, the Eligible Local Business will pay the Peer Contributor a 2% prepayment fee on the principal balance. The prepayment fee will be 1% for a prepayment of principal on or after the second and before the third conversion date and 0% on or after the third conversion date until the final maturity. No prepayment fee will be payable if the maturity date is accelerated following the occurrence of an event of default. Any prepayment of the Note must be made of 100% of the outstanding principal balance, plus any accrued and unpaid interest as of the date of redemption. Any redemption of the Note must be made in full.

**Remedies:** While the Note remains outstanding, the occurrence of any of the following events of default will result in the automatic acceleration of the maturity date, at which point all amounts due and owing under the Note will be immediately due and payable. The events of default will be limited to the following:

- Interest due remains unpaid for three (3) consecutive quarters.
- The qualified business ceases operations for more than sixty (60) days.
- The qualified business is insolvent or files for bankruptcy.

- Sale of the business or sale of all or a majority of the voting control of the business.
- Fraud or misappropriation of assets of the business by the eligible Local Business' equityholders.
- Loss of necessary licenses material to the business.
- Felony conviction of any of the Eligible Local Business' equityholders.
- Such other events of default as set forth in the Program Guide.

If the Note remains unpaid sixty (60) days after the final maturity date, then the Peer Contributor has the option to instruct the C2B Platform as agent to assign the Note to the Sponsor for payment on Program Support as provided below.

**Program Support:** For certain qualified investments, the Sponsor will guarantee to a Peer Contributor the following amounts: (1) all accrued and unpaid interest on the Note through the date of assignment and (2) 50% of the outstanding unpaid principal balance of the Note. Once assigned to the Sponsor the Peer Contributor will have no further rights to payment from the Eligible Local Business. The Sponsor may pursue payment of the assigned Note from the Eligible Local Business following the assignment of the Note to the Sponsor.

**Transferability:** Subject to certain securities law-related restrictions, the Note issued by the Eligible Local Business to the Peer Contributor will be transferable through the C2B Platform to Peer Contributors subject to limitations set forth in the Program Criteria.

**Reporting Requirements:** So long as the Note remains outstanding, the Eligible Local Business will submit to the Sponsor (which information will be made available to the Peer Contributor upon request) through the C2B Platform:

- Semi-annual (a) unaudited financial statements and (b) a supplemental report describing local business lending activity in the format prescribed by the Program Criteria, in each case no later than thirty (30) days after the end of the second quarter.
- Annually, the amount of total income, total taxable income and total tax or equivalent line items, reported on the business' federal tax forms for the most recently completed year, certified by the business' chief executive officer, or equivalent, and financial statements certified by the same officer. If financial statements of the issuer are available that have either been reviewed or audited by a public accountant, then, those financial statements can be provided instead of other financial information. This information shall be provided by no later than one-hundred twenty (120) days after the end of each fiscal year;

and (b) an annual lending survey in a format prescribed by the Program Criteria.

- Any additional notices of an event material to the Eligible Local Business' business.

**Certifications:**

So long as the Note is outstanding, the Eligible Local Business will provide the following certifications to the Peer Contributors and the Sponsor through the C2B Platform:

- Semi-annually, the qualified business' most senior officer or its equivalent will certify to its Peer Contributors and the Sponsor that information provided in the submitted financial statements and supplement report is accurate.
- Annually, the principal and the Eligible Local Business will make certifications about their continued status as an Eligible Local Business and continued satisfaction of the Program Criteria.

**Additional Considerations:**

This document does not create a binding legal obligation. A binding obligation shall only arise pursuant to duly executed definitive documentation and the requirement of the Program Guide.