

**Agenda Item # 4 UPDATED**  
**10/23/09 Finance Subcommittee Meeting**

**REMCHO, JOHANSEN & PURCELL, LLP**  
ATTORNEYS AT LAW

201 DOLORES AVENUE  
SAN LEANDRO, CA 94577  
PHONE: (510) 346-6200  
FAX: (510) 346-6201  
EMAIL: harrison@rjp.com  
WEBSITE: www.rjp.com

SACRAMENTO PHONE: (916) 264-1818

Joseph Remcho (1944-2003)  
Robin B. Johansen  
Kathleen J. Purcell (Ret.)  
James C. Harrison  
Thomas A. Willis  
Karen Getman  
Margaret R. Prinzing  
Kari Krogseng

**MEMORANDUM**

**To:** Members, Finance Subcommittee  
California Institute for Regenerative Medicine

**From:** James C. Harrison

**Date:** October 19, 2009

**Re:** Policy Options for Financial Review of Loan Applications

---

**INTRODUCTION**

The Disease Team Research Awards program is CIRM's first research program for which loans are available. CIRM has retained Square 1 Bank to assist CIRM in conducting a financial review of loan applications, based on financial information provided by the applicants to CIRM as part of their Disease Research Team Award applications. The Loan Administration Policy, which the Board adopted on January 30, 2009, contemplates that CIRM will review the analysis provided by CIRM's financial consultant or delegated underwriter in making a determination whether an applicant is financially qualified to receive a CIRM loan, including whether an applicant is eligible for a recourse loan or a non-recourse loan. CIRM staff has developed criteria for determining whether an applicant is eligible, on a financial basis, for a recourse loan. These criteria will be presented separately to the Finance Subcommittee for its consideration.

This memorandum describes the three basic options available for the review and determination of financial eligibility for a CIRM loan award. Each of these options would involve reviewing confidential financial information and analysis provided by CIRM's financial consultant or delegated underwriter, considering the input of the Grants Working Group regarding the technical scientific merit of the applicant's proposal and the quality of the applicant's scientific management team, including its investigators, researchers, and consultants,

and reporting back to the Grants Working Group. The three basic options are to: (1) delegate responsibility for the review and determination of eligibility, and the authority to negotiate any conditions, to CIRM staff; (2) delegate responsibility for the review and determination of eligibility, and the authority to negotiate any conditions, to the Finance Subcommittee; or (3) undertake the review and determination of eligibility at the Board.

The Board Executive Committee has considered each of these options and recommends a hybrid approach whereby CIRM staff would be delegated the authority to determine whether an applicant is eligible for a loan and to negotiate conditions, except where: (1) CIRM staff determines that an applicant for a recourse loan is only eligible for a non-recourse loan; (2) CIRM staff determines that an applicant for a recourse or non-recourse loan is not eligible for a CIRM loan award; (3) CIRM staff has offered a loan with conditions which the applicant has refused; or (4) where the Chair of the Board or the Chair of the Finance Subcommittee, in consultation with CIRM staff, determines that the terms of a loan should be subject to review by the Finance Subcommittee. Under these circumstances, the Finance Subcommittee would review the staff's recommendation and make a determination regarding the loan terms. The Board, of course, will make the final decision about whether to fund a loan.

### **BACKGROUND**

Pursuant to the Loan Administration Policy (the "LAP"), which was adopted on January 30, 2009, and which became effective as an interim regulation on June 15, 2009, an applicant for a loan must specify whether it is applying for a recourse loan or a non-recourse loan. The LAP defines a "recourse loan" as a "loan which the Loan Recipient organization is obligated to repay, notwithstanding the status of the CIRM-funded project." A "non-recourse" loan is defined as a "loan which the Loan Recipient organization is obligated to repay, subject to suspension or forgiveness of all or part of the loan based on the status of the CIRM-funded project." The LAP requires the recipient of a recourse loan to repay CIRM, with accrued interest, regardless of the success of the CIRM-funded project. The recipient of a non-recourse loan, by contrast, may request forgiveness of the loan under circumstances specified in the LAP. As a premium for CIRM's risk, the recipient of a non-recourse loan is required to provide CIRM with warrants equal to the *lesser* of 100% of the amount of the loan or 20% of the loan recipient's shares, on a fully diluted basis. Recipients of recourse loans are required to provide CIRM with warrant coverage equal to 10% of the amount of the loan. Finally, the LAP provides that an applicant for a recourse loan must indicate whether it would accept a non-recourse loan if CIRM determines that the applicant "does not meet the credit standards for Recourse Loans."<sup>1</sup>

---

<sup>1</sup> Because this provision would require an applicant to make a decision about whether it would accept a non-recourse loan before it knows whether it is eligible for a recourse loan, the Board Executive Committee recommends amending the LAP to eliminate this requirement. This will be discussed as part of Item 5.

The LAP states that “[e]valuation of applications for Recourse Loans will consider the ability of the applicant organization to repay the loan.”

CIRM staff has developed criteria (see Item 3) for determining whether an applicant qualifies for a recourse loan. Below, we discuss the options for evaluating loan applications and determining whether an applicant is financially eligible for a CIRM loan award.

### ANALYSIS

Pursuant to the Disease Research Team Awards program, CIRM has requested that applicants for loans provide financial information as part of their application for an award. CIRM staff has provided this information to Square 1, CIRM’s financial consultant, for analysis. The determination regarding eligibility for a CIRM loan will involve reviewing confidential financial information and analysis provided by CIRM’s financial consultant or delegated underwriter and CIRM staff analysis. In addition, the review and determination will involve input provided by the Grants Working Group regarding the scientific merit of an applicant’s proposal, as well as the strengths and weaknesses of an applicant’s scientific management team, including investigators, researchers, and consultants.<sup>2</sup> Regardless of the option that is selected, the analysis of the delegated underwriter, the staff’s analysis, and the action of the Finance Subcommittee and/or the Board will be reported to the Administrative Chair and Vice Chair of the Grants Working Group to provide benchmark information for future loans.

There are three basic options for conducting this review and determining an applicant’s eligibility.

(1.) CIRM staff could conduct the financial review based on confidential financial information and analysis provided by CIRM’s delegated underwriter or financial consultant and the input of the Grants Working Group, apply the “recourse” criteria, and make the determination regarding loan terms, including the type of loan (recourse vs. non-recourse). The ultimate decision to approve the application, of course, would rest with the Board. This option is consistent with CIRM’s evaluation of eligibility for CIRM grants and is consistent with CIRM’s administrative practices.

---

<sup>2</sup> In order to streamline the process for obtaining input from the Grants Working Group, CIRM staff would coordinate with the Administrative Chair and Vice Chair of the Grants Working Group, along with the Chairman, who is an ex officio member of the Grants Working Group.

(2.) Alternatively, the Board could delegate to the Finance Subcommittee the authority to conduct the financial review and make the determination regarding loan terms, including the type of loan. Again, the Board would make the final decision about whether to approve the application. This option would permit CIRM to draw upon the expertise of the members of the Finance Subcommittee; which could be useful during the infancy of the program, but ultimately may be cumbersome and time-consuming.

(3.) Finally, the Board itself could conduct the financial review, apply the “recourse” criteria, and make the determination regarding whether to award a loan and on what terms. Given the size of the Board and the complexity of the financial issues, this approach may be unwieldy and cumbersome.

### **HYBRID RECOMMENDATION**

After a full discussion of the relative merits of each of these options, the Board Executive Committee has recommended that the Board adopt a hybrid approach. Under this proposal, CIRM staff would review and evaluate the information provided by CIRM’s delegated underwriter or financial consultant and the Grants Working Group, determine whether an applicant is eligible for a recourse loan or a non-recourse loan, and negotiate any conditions. The staff’s determination would be subject to the review of the Finance Subcommittee only where: (1) CIRM staff determines that an applicant for a recourse loan is only eligible for a non-recourse loan; (2) CIRM staff determines that an applicant for a recourse or non-recourse loan is not eligible for a CIRM loan award; (3) CIRM staff has offered a loan with conditions which the applicant has refused; or (4) where the Chair of the Board or the Chair of the Finance Subcommittee, in consultation with CIRM staff, determines that the terms of a loan should be subject to review by the Finance Subcommittee. The analysis of the delegated underwriter, the staff’s analysis, and the action of the Finance Subcommittee and/or the Board will be reported to the Administrative Chair and Vice Chair of the Grants Working Group to provide benchmark information for future loans.

### **CONCLUSION**

The Board Executive Committee requests that the Finance Subcommittee recommend approval to the Board of the hybrid option described above. In order to build in flexibility and ensure that critical timelines are met, in the event that the Board does not adopt this recommendation, the Board executive committee also recommends that the Finance Subcommittee review the staff analysis and determination and make a conditional recommendation regarding loan terms to the Board, which would only be considered if the Board were to adopt the second or third option (Finance Subcommittee or Board evaluation and

Members, Finance Subcommittee  
October 19, 2009  
Page 5

determination). If the Board were to adopt the third option, the Board would make the final determination, if necessary, at the October 27-28 meeting. Of course, if the Board were to approve the criteria and delegate the responsibility for the financial evaluation of loan applicants either to CIRM staff or the Finance Subcommittee, the Board would not be required to consider the application of the criteria to the pending application or applications; rather, its funding decision would incorporate the prior determination.