

MEMO

TO: MAGIC Fund Screening Committee and City Council
FROM: Brekka Kramer, MACEDC President | CEO
DATE: September 25, 2023
SUBJECT: MAGIC Fund Request – Hot Switch Heating Systems, LLC

1. Request

Hot Switch Heating Systems, LLC (under Fiberglass Specialties in Minot, N.D.) has been approved by United Community Bank of ND/Bravera for a PACE loan. Through the MAGIC Fund, the business is looking to secure the community's portion of the interest buydown; this portion is \$215,384.65. BND will provide their portion of this 65/35 split in the amount of \$400,000, as an interest buydown.

2. Background

Hot Switch Heating Systems: Rooted in the mission "we keep trains moving", Hot Switch Heating Systems is dedicated to revolutionizing the rail switch heating sector. Founded in 2015 by two visionaries in Jacksonville, FL, the company is a pioneer in using induction heating to keep railroad tracks clear of snow and ice. After merging with Fiberglass Specialties in 2023, the combined strengths of both brands now serve as a one-stop solution for railroad switch heating.

The primary aim of this merger and associated expansion is to scale up the production of the Hot Switch Heating System, marrying it with the fiberglass switch cover system from Fiberglass Specialties. This project seeks to relocate and centralize production in Minot.

3. Project Description

Hot Switch Heating Systems has already made its mark with associations such as Norfolk Southern, Alaska Rail, and TranStar Rail. Looking forward, the company is setting its sights on securing significant projects in major hubs like New York City and Washington, D.C. The goal of this merger and expansion is to make Hot Switch the gold standard for rail switch heating across North America, targeting the more than seventy thousand switches of both major railroads and city metro systems.

In the immediate horizon, Hot Switch aims to hire two full-time employees for production and system build outs. As the production scales and revenue targets are achieved, the company intends to employ additional roles in sales, production, and research within the next five years.

Centralizing production in Minot will not only boost the local economy through job creation and bringing wealth from outside North Dakota but also maintains Minot's heart and long history as a hub for innovative rail solutions.

Backed by a moat of patents and a unique value proposition, Hot Switch is poised for market leadership. As the sole provider of induction heating for rails, coupled with Fiberglass Specialties' switch covers, the company is well positioned to capture a significant market share, promising sustainable growth.

This support from the MAGIC Fund will significantly reduce the cost of capital, allowing Hot Switch Heating Systems to reinvest more into job creation, R&D, and marketing. Over the span of the loan, this interest buy-down would result in savings of more than \$600,000 directly contributing to company growth and community benefits.

The loans being requested are for an approximately \$3.5 million project. See attached documents for additional description and paperwork associated with Hot Switch Heating Systems, LLC.

4. Financing

Bank Loan:	\$3,150,000
Personal Investment:	\$350,100
Total Sources:	\$3,500,100

5. Screening Process

A detailed screening process is executed by the Minot Area Chamber EDC when an application is received for MAGIC Fund dollars. This includes reviewing roughly nine key elements that are expressed in the MAGIC Fund Guidelines.

Pages 2 and 3 of the guidelines include the following items we have deemed important for the review process:

1. For use in economic and industrial development
 - o MACEDC has determined that this Hot Switch Heating Systems application meets this requirement.
2. To businesses that desire to expand or locate in the greater Minot trade area



- MACEDC has determined that this Hot Switch Heating Systems application meets this requirement.
- 3. Financing projects to support business growth in the primary Sectors OR Capitalization of revolving loan funds dedicated to addressing financing needs of small businesses not available through traditional financial institutions OR Marketing directly connected to attraction of opportunities to accomplish business growth in the Primary Sectors and use of capitalized small business revolving loan funds.
 - Hot Switch Heating Systems is a Primary Sector company as recognized through an application process through the North Dakota Department of Commerce. The business plan and conversations with the business applicant indicate that the business will attract a majority of its profit from outside of the state. MACEDC readily agrees with this qualification.
- 4. **MUST** support one or more of the following goals:
 - Create new jobs
 - Save existing jobs
 - Expand the local tax base
 - Increase capital investments
 - Improve the entrepreneurial climate of the region
 - MACEDC agrees with Hot Switch Heating Systems' assertions in their application that they will be creating new jobs, expanding the local tax base and increasing capital investment into a growing Minot area company.
- 5. **MAY** be used for workforce development to attract workers to meet workforce deficiencies within the Primary Sectors OR small business revolving loan funds
 - This item does not apply to this application. Hot Switch Heating Systems is not asking for workforce development funding.
- 6. Non-profit organizations will be considered for these funds only when it can be determined that the non-profit venture meets a purpose and goal for which the MAGIC Fund can be used based on these guidelines.
 - Hot Switch Heating Systems is a private, for-profit company and this section of the guidelines does not apply to them.

(The following items are found on page 9, under the Application Review Guidance section)

- 7. The following guidelines are intended to serve as a source of general guidance for Committee members in the administration of this program. It is important to note that the economic development needs of the area are such that a large degree of procedural flexibility is necessary to capitalize on windows of opportunity. In that context, administration of the MAGIC Fund must be dynamic enough to insure that the monies made available by this tax are prudently applied to



the economic development needs of the area consistent with the guidelines and policies of the MAGIC Fund and policy guidance established and regularly updated by the City Council.

- MACEDC views the Hot Switch Heating Systems request for MAGIC Fund support as the clearest use of these funds and has one of the least needs for procedural flexibility.
- 8. The acid test of the value of an application will be the relative positive “impact mix” of the business on the economy of the region.
 - The number of jobs created or saved
 - Quality of those jobs
 - Expansion of the tax base
 - Financial mix (level of owner’s equity)
 - Organizational growth potential
 - Environmental impact
 - Use of regional materials in production process
 - Amount of third-party participation
 - Amount of primary money generated by the project
- The referenced acid test takes in to account a variety of factors tied to the value of an application – one could look at this test as “What is the ROI/Impact of giving these funds to this particular project?” Much of the return on a \$215,384.65 request (forgivable loan) comes out in measurable items that would be included in a development agreement. MACEDC has laid out recommendations to measure the ROI tied to this request.
- 9. MUST be clear, measurable performance benchmarks to regularly monitor compliance and performance.
 - Assuming that there are clear, measurable benchmarks in a BIA, and that they are agreed to by all parties, then this section of the review would be satisfied. Due to the low-risk nature of participating in the BND PACE program, MACEDC proposes a 3-year developer agreement to track growth and use of the funds.

6. Recommendation

It is the recommendation of the Minot Area Chamber EDC to support this MAGIC Fund request. As a part of the request, we would ask for the \$215,384.65 in PACE interest loan buydown from the MAGIC Fund Steering Committee and the Minot City Council for Hot Switch Heating Systems.

The MAGIC Fund has been used for efforts of this sort many times in the past. This application represents one of the lowest risks for the MAGIC Fund to aid growth within a primary sector company that employs nearly a dozen individuals in our community. The local bank and BND have gone through their underwriting criteria and credit analysis of the borrower and deemed them to be eligible.

Regarding stewardship for the MAGIC Funds, Minot Area Chamber EDC recommends that project tracking procedures associated with the development agreement include the number of new employees



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tied to Hot Switch Heating Systems and the continued operation of the new line of business at the end of each year. These funds would be structured as a forgivable loan, should these metrics be met.

End of year 1	Total employees as a result of the merger – 2
End of year 2	Total employees as a result of the merger – 3
End of year 3	Total employees as a result of the merger – 3