

Date of Hearing: April 29, 2015

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT, AND THE ECONOMY

Eduardo Garcia, Chair

AB 1393 (Burke) – As Introduced February 27, 2015

SUBJECT: California Pollution Control Financing Authority

SUMMARY: Expands the authority and program focus of the California Pollution Control Financing Authority (CPCFA) from providing financial assistance to address the control and remediation of pollution and the capital access challenges of small businesses to offering unlimited types of financial products to an expansive list of public and private entities, as specified. Specifically, **this bill:**

- 1) Expands the type of financial assistance CPCFA can offer to support a broad range of pollution control project financing activities from loans and the issuance of bonds and notes to any type of financial assistance including, but not limited to, grants, loans, credit enhancements, and other incentives.
- 2) Expands the types of financial products that CPCFA can offer under the alternative funding source program of the California Capital Access Program (CalCAP) including, but not limited to, a loss reserve program that benefits any person, company, corporation, public agency, partnership, or firm engaged in activities in the state that requires financing.
- 3) Expands CPCFA's authority to adopt new program guidelines using emergency regulation authority from its loan loss reserve program to any financial assistance program using a funding source other than the CPCFA including, but not limited to, a loss reserve program that benefits any person, company, corporation, public agency, partnership, or firm engaged in activities in the state that require financing.
- 4) Strikes obsolete program authority and associated provisions relating to a grant and loan program for neighborhoods with high poverty or unemployment levels for the purpose of assisting cities and counties in developing and implementing growth policies and programs that reduce pollution hazards, promote infill development, and to revitalize these communities. These provisions sunset on January 1, 2012.
- 5) Makes other technical and conforming changes.

EXISTING LAW:

- 1) Establishes the CPCFA with specified powers and duties, and authorizes the authority to approve financing for pollution control projects and facilities, administer a loss reserve program for small businesses, and provide grants and loans to remediate brownfields.
- 2) Defines “participating party” for the purposes of financing pollution control, remediation, and elimination projects to mean any person, company, corporation, public agency, partnership, firm, or other entity or group of entities engaged in operations within this state that requires financing.
- 3) Establishes CalCAP for the purpose of providing a small business loss reserve account program through participating financial institutions. As part of implementing the program, the CPCFA establishes a loss reserve account for each participating financial institution.

- 4) Authorizes CalCAP to adopt alternative loss reserve programs using a funding source other than those of the CPCFA.

FISCAL EFFECT: Unknown

POLICY ISSUE FRAME:

The CPCFA is one of nine independent financing authorities, chaired by the State Treasurer. Initially established in 1975, the CPCFA was as part of the broader modernization of the State Treasurer's Office under State Treasurer Jesse Unruh. With the Tax Reform Act of 1986 and the rise in the use of private activity bonds, the CPCFA was able to play a major role in establishing a cost-effective means for using tax exempt bonds to fund important pollution control projects and facilities.

Today, however, pollution control private activity bonds are not as much in demand and the CPCFA's work on brownfields has lessened, according to its annual reports. The most active program at the CPCFA is CalCAP. AB 1393 proposes to leverage CalCAP's current statutory authority and financing expertise to help other public and private entities meet their unique financing needs. In implementing these statutory changes, CPCFA is requesting very broad program authority in order to respond to current and potential future financial opportunities.

The Comment section of the analysis includes additional information on CPCFA and its reduced mission-related programs, the increasing success of the CalCAP Program, and examples of the types of initiatives currently being undertaken through CPCFA's alternative funding source programs. The analysis comments also raise issues about the scale of the proposed program flexibility. Amendments are recommended in comment 6 of the analysis to provide greater program transparency and accountability within the broader financial assistance framework.

COMMENTS:

- 1) **Author's Purpose:** According to the author, "The California Capital Access Program (CalCAP) provides loans to qualifying small businesses that might not otherwise be able to obtain a loan. In addition to their support for small businesses, their financing has been critical for several of our clean air and energy efficiency programs. For example, the Air Resources Board has utilized CalCAP to help businesses invest in newer, cleaner trucks, and, together with the California Energy Commission, the program will also provide financing for electric vehicle charging stations.

AB 1393 will build on the success of the CalCAP program and allow the program to provide loans and credit enhancement to individual consumers. If we're going to meet our carbon emission reduction goals, we'll need to broaden our outreach and support. By expanding CalCAP, California will be able to partner with financial institutions to help the programs funded by our Cap and Trade resources reach communities and consumers that may never have been able to reduce their carbon footprint and energy use without a little help."

- 2) **Independent Financing Authorities:** The CPCFA is one of nine independent financing authorities including the:

- California Alternative Energy and Advanced Transportation Financing Authority
- California Educational Facilities Authority

- California Health Facilities Financing Authority
- California Healthy Food Financing Initiative Council
- California Industrial Development Financing Advisory Commission
- California Pollution Control Financing Authority
- California School Finance Authority
- California Tax Credit Allocation Committee
- California Transportation Financing Authority

In general, each of the authorities is governed by a core set of three board members: The State Controller, the Department of Finance, and the State Treasurer, who serves as the Chair of each of these boards. In some cases, the core set of members serve as the entirety of the financing authority board. In other cases, the core members are joined by additional state officials based on one or more missions of the authority. The Chair of the Energy Commission and the President of the Public Utilities Commission are, as an example, members of the California Alternative Energy and Advanced Transportation Financing Authority.

While a majority of these boards were initially established to serve specific public works and private sector bond financing functions, their current activities have grown far beyond the construction of schools, hospitals, and pollution control facilities. Over the years, as financial markets changed and the Legislature saw opportunities to create niche programs, the core missions of the financing authorities expanded and additional financing authorities were even created.

Today, the missions of the various financing authorities sometimes overlap, as well as the tools the financing authorities have been provided. In March 2015 the California Energy Commission approved spending AB 118 funds for the Electric Vehicle Charging Station Financing Program and will be using the CPCFA as its finance administrator. Mission-wise, this partnership seems more appropriate for the California Alternative Energy and Advanced Transportation Financing Authority.

However, given CPCFA's demonstrated ability to design financial products that both meet the requirements of the public agency and the private sector it is not surprising that the Energy Commission and the Air Resource's Board (ARB) have chosen CPCFA. Organizationally, however, it draws into question why the state needs nine separate authorities or whether the current programs could be divvied up more effectively between six financing authorities.

- 3) **California Pollution Control Financing Authority:** The CPCFA was established in 1972 as an independent financing authority for the purpose of providing a revenue bond based method of efficiently financing pollution control facilities. CPCFA's role as a conduit revenue bond issuer has expanded over the years to also include a now defunct sustainable communities grant program; CalCAP, a small business loss reserve program; and the California Recycle Underutilized Sites Program, which provides grants and loans to support the remediation of brownfield sites.

One component of CPCFA's funding is provided through an assessment on large businesses that utilize the CPCFA as a conduit bond issuer. Bond issuance fees vary based on the size of business and the size of the issuance. The maximum fee is 0.0066 on the face value of the bonds. These fees are then redirected by the CPCFA board for mission-related purposes. Small businesses, as an example, can receive up to \$205,000 towards the cost of their own bond issuance.

In 2013, the CPCFA board voted to waive the fee, as tax exempt bond financing began to weaken. In May 2015, the CPCFA board will vote on extending the waiver of the fee to the end of 2015.

Currently, CPCFA's has \$3.5 billion in unused carryover tax exempt authority and a cash balance of \$15.3 billion within its bond program.

In 2014, the CPCFA's California Pollution Control Tax Exempt Bond Financing Program received 6 applications for a total of \$198 million. Final resolutions were approved for six projects including financing for Athens Services (\$138 million), Mill Valley Refuse Services, Inc (\$4.7 million), and Sierra Pacific Industries (\$30 million). Eight bond issues were sold in 2014 for a total amount of \$260.6 million.

- Total bonds sold over the lifetime of the program: \$14 billion
- Outstanding bonds (3/31/2015): \$3 billion

Another key program of the CPCFA is the California Recycle Underutilized Sites Program, which was developed to encourage and assist in the redevelopment of brownfield sites. As initially conceived, the CPCFA would be one of three public entities funding brownfield remediation projects. Today, those other programs have been brought in-house resulting in the CPCFA financing both the assessment and a remediation of the brownfields project. The assessment component provides low-cost loans to finance professional site assessments and the remediation component provides low-cost loans and grants to finance brownfield clean-up activities. Since inception, 74 projects have been funded for a total of \$59 million including 44 assessment loans and 29 grants and one loan to finance remediation work. In the first quarter of 2014, \$2.5 million was awarded to brownfield projects.

According to the program's 2013 Annual Report, the financing of brownfield clean-up projects is slowing for a variety of reasons including the complexity and risks associated with the work. CPCFA staff transferred \$4 million of assessment loan funds back to its general purpose fund to support other programs in 2013.

- 4) **California Capital Access Program for Small Businesses:** CalCAP was established by legislation enacted in 1994 for the purpose of incentivizing financial institutions to provide small businesses with the capital to maintain and grow their business. The program uses a portfolio-based credit enhancement model, whereby a loss reserve fund is established with the participating lender to offset potential losses of enrolled small business loans.

Unlike a loan guarantee which ensures payment in the case of default on a certain percentage of the value of the loan, under the loss reserve fund model, the lender has access to the full loss reserve account and can recover 100% of the default, if sufficient moneys are in the account. The model encourages lenders to maintain good underwriting practices because using the loss reserve often can quickly draw-down the reserve leaving little for other potential defaults within the portfolio.

CalCAP loans can be used to finance the acquisition of land, construction or renovation of buildings, the purchase of equipment, other capital projects and working capital. There are some limitations on real estate loans and loan refinancing. The maximum loan amount is \$2.5 million. The maximum premium lenders will pay is \$100,000 (per borrower). Lenders set the terms and conditions of the loans and decide which loans to enroll into CalCAP. Loan fees, which are used to capitalize the loan reserve account, are set by the lender and are in the range of 2% to 3.5% of the total loan amount. Loans can be short- or long-term, have fixed or variable rates, be secured or unsecured, and bear any type of amortization schedule.

In 2013, CalCAP had 38 lenders enrolled in the loss reserve program. These lenders enrolled 3,236 small business loans, representing \$205 million in loans. This was a 39% increase in the number of loans and a 63% increase in the amount of money loaned from the prior year. Approximately \$32 million was deposited into participating lenders' loan loss reserve accounts. CPCFA processed and approved 109 claims from lenders against their loss reserve accounts with \$2.6 million paid out as a result. According to the State Treasurer's website (04/26/2015), since inception, CalCAP has enrolled 17,202 loans. The average CalCAP loan was \$60,988.

Moneys to operate CalCAP originally came from excess bond issuance fees, discussed in a prior comment. From 2004 to 2010, about \$35 million was used to finance CalCAP. In 2010, CalCAP received its first General Fund moneys as part of a comprehensive \$32 million small business budget proposal and in 2011 CalCAP was chosen to administer a portion of federal funds for a small business access to capital program. Currently, CalCAP operates almost exclusively on funds received from its alternative funding source loss reserve program.

CalCAP is currently or has operated a number of alternative funding source programs for the ARB including the On-Road Heavy-Duty Diesel Vehicle Program for small business truck owners and a Proposition 1B Loan Assistance Program to help finance 2007 or newer heavy-duty diesel or LNG fueled trucks. As noted earlier in the analysis, the Energy Commission has recently approved an MOU with CPCFA to help finance electric vehicle charging stations.

According to the CPCFA, one of the reasons the State Treasurer (sponsor) sought the introduction of AB 1393 was to pursue another financial arrangement with the ARB. This time to have CPCFA administer an alternative funding source program involving residential customers. Under CPCFA's current statutory structure, the alternative funding source program could narrowly be interpreted to only allow small business loss reserve programs with only minor alternation. The CPCFA seeks greater program flexibility to assist the ARB and other public and private entities through the implementation of AB 1393.

- 5) **State Small Businesses Credit Initiative:** In October 2010, Congress passed and the President signed the Small Business Jobs Act. Among other things, the Act created the State Small Business Credit Initiative (SSBCI), which is authorized to expend up to \$1.5 billion for state sponsored small business finance programs. Over the life of this program, every federal dollar must be matched by \$10 from the private sector -- the deadline for using the funds is September 2017. Also, funding for program administration, outreach, and oversight is primarily the responsibility of the state.

Under the SBCCI funding formula, California is eligible to receive up to \$168 million, which is the largest amount of any state. California uses its moneys to capitalize the Small Business Loan Guarantee Program at the I-Bank's Small Business Finance Center and the California Capital Access Program (CalCAP) loan loss reserve program and a collateral support program administered through the California Pollution Control Financing Authority.

California has received \$110 million of the total \$168 million available and, as of June 30, 2014, the state has encumbered roughly \$87.6 million with approximately \$40.6 million set aside to cover loan guarantees; \$7.2 million deposited with private financial institutions through the CalCap and \$39.8 million used for the collateral support program. Approximately \$2.4 million has been used for direct administrative costs, resulting in a cumulative 2.18% administrative cost per dollar allocated by the U.S. Treasury. Since inception, 47,202 jobs have been created (7,372 jobs) or retained (39,830 jobs) by the close of 2013. 2014 job impacts were 2,228 new jobs and 13,931 retained jobs.

One of the unique features of the federal SSBIC program is that once the state meets the 10:1 leverage, the state is authorized to reuse those funds for other purposes. Under AB 1393, the CPCFA would be authorized, unless federal regulations prohibited, to use those federal funds to benefit any person, company, corporation, public agency, partnership, or firm engaged in activities in California that requires financing. As currently drafted, there would be very limited control on the re-use of those funds. While clearly not the intent of the sponsor or the CPCFA, as currently drafted the bill is overly broad.

- 6) **Proposed Amendments:** Below is a list of amendments the author may wish to consider when bringing the bill before the committee:
- a) Define eligible types of financial assistance for pollution control projects. [*current bills says "including , but not limited to"*]
 - b) Define eligible types of financial assistance for the alternative provisions of the loss reserve program. [*current bills says "including , but not limited to"*]
 - c) Provide a policy focus for the non-small business programs that may be offered through the alternative funding source program, such as pollution control, natural resource preservation, and/or renewable energy. [*Current bill authorizes the CPCFA to meet any financing need*]
 - d) Define participating party for the alternative funding source provisions of the loss reserve program. [*To the extent that the alternative program is going to be an increasing activity of CPCFA, it would be helpful to have those statutory provisions be more integrated into the overall statute.*]
 - e) Require notice to the Joint Budget Committee and the related oversight policy committees when undertaking an alternative funding source project including the source of the funding, the public agency that is providing the capital, and legislative reference, if appropriate.
 - f) Expand the existing CalCAP reporting requirement that relates to small businesses to be expanded to include financing activities related to the alternative funding source provisions.
 - g) Sunset the expanded authority on or before January 1, 2021.
- 7) **Related Legislation:** Below is a list of bills from the current and prior sessions.
- **AB 826 (Gipson) Small Business Export Insurance:** This bill expands the types of financial products the Small Business Finance Center, located within the California Infrastructure and Economic Development Bank, may offer small business to include insurance and co-insurance for the purpose of increasing export activities. Status: Pending in the Assembly Committee on Appropriations.
 - **AB 850 (Nazarian) Publicly Owned Utilities:** Authorized joint power authorities to issue rate reduction bonds to finance publicly owned utility projects until December 31, 2020. The bonds are to be secured by utility project property and repaid through a separate utility project charge imposed on the utility customers' bills. While the bonds are issued by the local joint power authorities, AB 850 included an additional state review process by the California Pollution Control Financing Authority (CPCFA). Status: Signed by the Governor, Chapter 636, Statutes of 2013.
 - **AB 901 (V. Manuel Pérez) Small Business Act Implementation:** This bill updates terms and makes clarifications to assist the successful implementation of the federal and state small business acts of 2010. Status: Signed by the Governor, Chapter 483, Statutes of 2011.

- **AB 981 (Hueso) California Capital Access Program:** This bill modifies the California Capital Access Program (CalCAP), administered through the California Pollution Control Finance Authority (CPCFA), in order to encourage greater participation by financial institutions in the small business credit program. Status: Signed by the Governor, Chapter 484, Statutes of 2011.
 - **AB 1632 (Blumenfeld) Capitalization of the California Capital Access Program:** This bill provides the necessary statutory changes in the area of job creation and small business development in order to implement the 2010 Budget Act. The bill transfers \$32.4 million from the General Fund to support four small-business and jobs programs that exist in current law. The funding appropriated in this bill goes to the Small Business Loan Guarantee Program (\$20 million); California Capital Access Fund (\$6 million); Small Business Development Centers (\$6 million); and the Federal Technology Centers (\$350,000). Status: Signed by the Governor, Chapter 731, Statutes of 2010.
 - **SB 225 (Simitian) California Capital Access Loan Program and Truck Retrofit Financing:** This bill authorizes the California Pollution Control Financing Authority to establish a loss reserve account program for the purposes of financing terminal rental adjustment clause leases. Status: Signed by the Governor, Chapter 492, Statutes of 2011.
 - **SB 832 (Senate Committee on Environmental Quality):** This bill makes a number of changes to the program changes to the authority and operations of the California Pollution Control Financing Authority. Among other things, the bill modifies the terms "project" and "pollution control facility", as defined in the California Pollution Control Financing Authority Act that are eligible for the sales and use tax exclusion and includes public agencies in the definition of "participating parties" that are eligible for financial assistance in connection with the projects designed to control or eliminate environmental pollution. Status: Signed by the Governor, Chapter 643, Statutes of 2009.
 - **SB 1311 (Simitian) Loss Reserve Modification:** This bill reduces the monetary contribution of the California Pollution Control Financing Authority to an amount equal to the amount of fees paid by a participating financial institution. Also provides that Authority may withdraw from the loss reserve account all interest or other income that has been credited to that account for the purpose offsetting administrative costs and contributions. Status: Signed by the Governor, Chapter 401, Statutes of 2008.
- 8) **Double Referral:** The Assembly Rules Committee has referred this measure to the Assembly Committee on Banking and Finance (Banking) and the Assembly Committee on Jobs, Economic Development and the Economy. This measure passed Banking on an 11 to 0 vote.

REGISTERED SUPPORT / OPPOSITION:

Support

California State Treasurer

Opposition

None received

Analysis Prepared by: Toni Symonds / J., E.D., & E. / (916) 319-2090