

Date of Hearing: April 21, 2009

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT AND THE
ECONOMY

V. Manuel Perez, Chair

AB 1009 (V. Manuel Perez) – As Introduced: February 27, 2009

SUBJECT: Small Business Direct Loan Program

SUMMARY: Authorizes the establishment of a direct loan program for the purpose of providing loans to qualified businesses, as specified. Specifically, this bill:

- 1) Expands the Small Business Loan Guarantee Program (SBLGP), administered by the Business, Transportation and Housing Agency (BTH), to include authority for offering direct loans.
- 2) Creates a separate account within the California Small Business Expansion Fund (Expansion Fund) for the purpose of this measure.
- 3) Requires the director of the SBLGP to develop and implement an application and review process that minimally includes eligibility standards, rating and ranking criteria, and other appropriate policies and procedures for evaluating direct loans, as specified.
- 4) Provides that the maximum loan amount under the program is \$500,000 and that all direct loans have a guarantee from a federal agency or department.
- 5) Requires that each applicant successfully demonstrates that they have reasonable access to business and management technical assistance during the term of the loan.
- 6) Requires information on the direct loan program be annually reported to the Legislature as part of an existing annual reporting requirement of SBLGP.
- 7) Requires an independent audit of the direct loan program and its findings be reported to the Governor and Legislature no later than January 1, 2012.

EXISTING LAW:

- 1) Provides that BTH oversee and coordinate the activities of various departments, offices, and economic development programs, with responsibility for maintaining the strength and efficiency of California's infrastructure and financial markets. These programs provide financial and programmatic regulation important to the economic marketplace, community development, and the safe and efficient flow of commerce.
- 2) Establishes the SBLGP within BTH for the purpose of assisting small businesses in obtaining long term loans or lines of credit from conventional financial institutions, which small businesses would not otherwise qualify for without the guarantee. Under this program, financial development corporations (FDCs) act as financial intermediaries between the state, the small business, and the financial institution.

- 3) Establishes the Expansion Fund for the purpose of retaining the moneys which separately capitalize the SBLGP and paying out defaulted loan guarantees issued under the SBLGP. Each account within the Expansion Fund is legally separate and is prohibited from securing loan guarantees or other obligations of another FDC. The state is not liable or obligated beyond the funds allocated and deposited in an individual trust fund account within the Expansion Fund.

FISCAL EFFECT: Unknown

COMMENTS:

- 1) Purpose: According to the author, California small businesses face many challenges during this current economic downturn. Debt markets are frozen, unemployment is rising, and production is stalled. Although the federal government is working aggressively to improve the flow of capital, the fact remains that many small businesses do not have sufficient access to necessary financial resources.

AB 1009 addresses this issue by authorizing the expansion of an existing state program to offer direct loans. The SBLGP has been operated by the state for over 20 years and has an established network of FDCs to undertake the expansion of the existing program to include direct loans. In fact, the SBLGP already provides direct loans for farmers who can secure a federal farm loan guarantee.

This bill is also implements a recommendation from the California Economic Development Recovery Strategy (Recovery Strategy) developed by the Assembly Committee on Jobs, Economic Development, and the Economy (JEDE).

- 2) California Small Business: California's dominance in many economic areas is based, in part, on the significant role small businesses play in the state's \$1.8 trillion economy. Businesses with less than 100 employees comprise more than 98.3% of all businesses, and are responsible for employing more than 57.9% of all workers in the state.

Small- and medium-sized businesses are crucial to the state's international competitiveness and an important means for dispersing the positive economic impacts of trade within the California economy. Of the over 52,000 companies that exported goods from California in 2006, 95% were small- and medium-sized enterprises (SME) with fewer than 500 employees. These SMEs generated nearly half (44%) of California's exports in 2006. Nationally, SMEs represented only 29% of total exports. Again, these numbers include the export of only goods and not services.

Small businesses function as economic engines, especially in challenging economic times. During the nation's economic downturn from 1999 to 2003, microenterprises (businesses with less than five employees) created 318,183 new jobs or 77% of all employment growth, while larger businesses with more than 50 employees lost over 444,000 jobs. From 2000 to 2001, microenterprises created 62,731 jobs in the state, accounting for nearly 64% of all new employment growth. Common types of microenterprises include engineering, computer system design, housekeeping, construction, landscaping, and personnel services.

During the current economic downturn, small businesses have been especially hard hit. A recent study by the National Small Business Association found that over a third of business owners expressed the most significant concern over access credit. Additionally, in the most recent American Express OPEN Economic Pulse Report, 63% of small businesses reported being impacted by tightening credit conditions. This is up from 50% just two months earlier. Until credit conditions rebound, it will be difficult for small businesses, the state's historic economic engines, to start expanding and creating jobs.

- 3) Small Business Direct and Guarantee Loan Program: The SBDGLP enables a small business to obtain a term loan or line of credit when it cannot otherwise qualify for a loan on its own. The state, working through 11 FDCs, offers direct loans or loan guarantees that a qualifying small business borrower could not otherwise obtain.

Applicants must meet the definition of a small business (100 or fewer employees) with the specific market rate loan terms and interest rates being negotiated between the borrower and the lender. Proceeds of the loan must be used primarily in California for any standard business purpose applicable to the applicant's business. The guarantee program provides guarantees covering up to 90% of the loan, but not exceeding \$500,000. The guarantee program allows a business to not only obtain a loan but to also establish credit with a lender. The business is then more likely to obtain additional financing on its own.

In 2007-08, approximately \$38 million was available for loan guarantees under the SBLGP, which leveraged \$169 million in small business loans. During this period, 1,358 guarantees were provided, creating and/or retaining 16,301 jobs. The total outstanding loan portfolio in 2007-08 was \$365 million, representing 2,437 outstanding guarantees.

- 4) California Economic Development Recovery Strategy: In anticipation of the enactment of the \$787 billion federal stimulus package, Assemblyman Pérez, Chairman of Economic Development Committee, called for the preparation of a 24 month blueprint on how to most effectively use federal stimulus funds to address the state's most immediate economic and workforce needs while still serving as a catalyst for advancing the state's long-term economic growth. In March 2009, the Recovery Strategy was published and is currently out for public comment.

The Recovery Strategy proposes to use the broadest set of community, economic, and workforce development tools to link these new federal resources with the people and organizations they are designed to serve. In order to accomplish this important task, the Recovery Strategy recommends that the state serve as a facilitator to support and enhance each community's individual initiative to design and implement policies and programs which best fit their needs. The recommended actions in the Recovery Strategy are organized around five community development goals. The five goals are to:

- Goal 1 – Improve business access to business capital
- Goal 2 – Target infrastructure projects that link to economic development
- Goal 3 - Expedite workforce services and training opportunities
- Goal 4 – Enhance local and regional community development capacity

- Goal 5 – Ensure that the state's recovery strategy is a plan for all Californians.

Each of these goals includes a list of specific action items, including actions that should start immediately, to actions proposed in the next six-to-12 months and, finally, those actions which will help to fortify the economy as the state begins to move out of the recession in the next 12-to-18 months.

The direct loan program proposed in AB 1009 is a specific recommendation under Goal #1 to have the state take actions to improve businesses access to capital.

- 5) Capitalizing a Direct Loan Program: While AB 1009 establishes a separate authority to offer direct loans under the SBLGP, the bill does not authorize sharing the current program's capitalization. In this way, AB 1009 does not dilute the impact of the existing program.

Implementation of AB 1009 will require its own capitalization, probably in the range of \$10 to \$20 million. These moneys could be an eligible cost under one or more of the federal stimulus programs. However, in order to access these moneys, the state would need to clearly demonstrate that it has the capacity and authority to implement such a program. AB 1009 provides such authority.

- 6) Author's amendments: Committee staff understands the author will be offering the following amendments:

- a) Require, as a condition of applying for a loan, that the business has not been successful in accessing capital in the private market.
- b) Require, as a condition of receiving a loan, that the business has the ability to repay the loan.
- c) Require the executive director to determine that the direct loan program is sufficiently capitalized prior to the program's commencement.
- d) Extend the sunset on the program from 2013 to 2015 to reflect the time it may take to capitalize the program.
- e) Make other technical and clarifying changes.

- 7) Related legislation: Below is a list of related legislation.

- a) AB 610 (Price): This bill enhances the Small Business Loan Guarantee Program's ability to leverage existing program dollars resulting in the ability to serve more small businesses financial needs per year. Status: Signed by the Governor, Chapter 601, Statutes of 2007.
- b) AB 1104 (Aghazarian): This bill makes modifications to the Small Business Loan Guarantee Program relating to small business disaster guarantees and eligible investments of SBLGP funds. Status: Signed by the Governor, Chapter 624, Statutes of 2007.

- c) AB 1431 (Arambula): This bill would have established the Early Stage Investment Guarantee Program, administered through the Small Business Loan Guarantee Program, for the purpose of assisting small businesses in attracting investors during the early years of their company's growth, as specified. Status: Died pursuant to Art. IV, Sec. 10(c) of the Constitution in 2008.

- d) SB 358(Ducheny): This bill authorizes the establishment of a Native American Business Revolving Loan and Guarantee Program, which would be administered through the SBLGP at BTH. The purpose of the program is to promote the long-term economic viability of tribal communities by providing capital to create or retain jobs, offer business development and employment training, and provide general education to tribal members. Status: Pending a hearing in the Senate Committee on Appropriations.

- e) SB 1200 (Ducheny): This bill would have authorized the establishment of the Native American Business Revolving Loan Program, which would be administered through the SBLGP at BTH. The purpose of the program is to promote the long-term economic viability of tribal communities by providing capital to create or retain jobs, offer business development and employment training, and provide general education to tribal members. Status: Held under submission in the Assembly Committee on Appropriations in 2008.

REGISTERED SUPPORT / OPPOSITION:

Support

Assembly Committee on Jobs, Economic Development, and the Economy (sponsor)
Association of Financial Development Corporations

Opposition

None received

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