

# CALIFORNIA INFRASTRUCTURE AND ECONOMIC DEVELOPMENT BANK

## SMALL BUSINESS FINANCE CENTER

### STAFF REPORT

#### DIRECTIVES AND REQUIREMENTS: PROPOSED REVISIONS

#### ISSUE:

The Small Business Financial Assistance Act of 2013 (the “Small Business Act”) governs the implementation of programs administered under the Small Business Finance Center (“the SBFC”) within the California Infrastructure and Economic Development Bank (“IBank”). In preparation for the receipt of a large amount of new funding under the State Small Business Credit Initiative (as discussed below), IBank staff carried out a complete review of the Directives and Requirements which govern the SBFC’s programs. The resulting proposed changes to the Directives and Requirements primarily affect the State and Federal funded Small Business Loan Guarantee Programs (“SBLGP”), as well as direct loan programs such as the Farm Loan Program and the Jump Start Loan Program, the Surety Bond Guarantee Program, the Secondary Market for Guaranteed Loans, the Disaster Relief Loan Guarantee Program and the Small Business Loan Catalyst Program; all of which are programs under the Small Business Finance Center. If other programs or other financing products are offered by the SBFC in the future, the Directives and Requirements may be supplemented to address those new programs and financing products. Pursuant to the discussion below, IBank staff recommends the IBank Board of Directors (the “Board”) approve Resolution No. 22-10, adopting Amended and Restated Directives and Requirements (the “A&R Directives and Requirements”) and approving the SSBCI Allocation Agreement.

#### BACKGROUND:

IBank was established pursuant to the Bergeson-Peace Infrastructure and Economic Development Bank Act (the “IBank Act”) for the purpose of providing financial assistance to eligible entities in the State of California (the “State”) through a variety of financing mechanisms. The California SBLGP was established in 1968 to provide access to capital for small businesses, create jobs and opportunities for small businesses, targeting those owned by minorities, women, and disabled persons. The Small Business Act was added to the IBank Act in 2013 to: (i) establish the SBFC within IBank, and (ii) transfer administration of the State’s small business financing programs (except those housed within the State Treasurer’s Office) to the SBFC.

The SBFC promotes statewide economic development by providing loan guarantees and direct loans to small businesses that have difficulty accessing capital. For loan guarantees, the loans are made by financial institutions, typically banks, credit unions and Community Development Financial Institutions (“CDFIs”), with the guarantee administered by Financial Development Corporations (“Corporations”) that contract with IBank. As a result of the SBFC, participating small businesses are able to secure financing that allows them to grow and expand their business. The SBLGP serves as a credit enhancement and an incentive for financial institutions to make loans to small businesses that otherwise may not be able to obtain financing. The SBLGP has supported over \$1.6 billion in loans since FY13/14. In addition, over 430,000 jobs have been created or retained with SBLGP assistance since the program inception.

In addition to the SBLGP and other loan guarantee programs, the SBFC has active direct loan programs, the Farm Loan Program and the Jump Start Loan Program. Through the Farm Loan Program, IBank loans money directly to participating Corporations to fund farm-related loans that are guaranteed by the U.S. Department of Agriculture (USDA). The loans provide capital for farm operating, equipment, and

ownership of family farms. To date, the SBFC has closed 88 Farm Loans in the program. Through the Jump Start Loan Program, IBank contracts with those Corporations that have proven experience with micro-lending in low-wealth communities to provide credit underwriting, loan disbursement and servicing of IBank-funded loans, as well as technical assistance and financial training to prospective small business borrowers under the Jump Start Program. Jump Start loans have provided over 1,820 hours of technical assistance to over 528 startups since program inception.

The State Small Business Credit Initiative (“SSBCI”) was originally created through federal legislation – President Obama’s Small Business Jobs Act of 2010. The initial SSBCI program was funded with \$1.5 billion to strengthen state programs that support financing of small businesses. California received \$168 million of the \$1.5 billion, which was shared between two state agencies focused on small business support – IBank for the SBLGP, and the California Pollution Control Financing Authority (“CPCFA”) within the State Treasurer’s Office, to manage the California Capital Access Loan Program (CalCAP) and the Collateral Support Program (CSP). The SBLGP received \$84.2 million from the initial SSBCI program (“SSBCI 1.0”), which was concluded in 2017. California was allocated \$167.8 million in SSBCI 1.0 to operate three credit support programs (SBLGP, CSP and CAP). Overall, with the infusion of federal monies, California supported 7,699 loans that generated \$793 million in total financing through the end of 2015. Between our three SSBCI programs this support created or retained over 70,000 jobs for Californians.

President Biden’s American Rescue Plan Act of 2021 reauthorized and funded a new version of the SSBCI program (“SSBCI 2.0”), providing a combined \$10 billion to states and Tribal governments to empower small businesses to access capital needed to invest in job-creating opportunities. The funds will also support promotion of American entrepreneurship and democratize access to startup capital across the country, including in underserved communities. Of the \$10 billion reauthorized, California is slated to be allocated approximately \$1.181 billion – to once again be split between IBank and CPCFA for their respective programs. As noted in our SSBCI 2.0 application, subject to increasing the maximum guarantee under the SBLGP from \$2.5 million to \$5 million, IBank anticipates supporting over \$535 million in small business lending per year, and over \$5 billion in the aggregate over the course of the ten-year program. We estimate this activity will create 78,698 jobs through 2031.

The SSBCI Allocation Agreement establishes the terms and conditions for the State to receive capital funds under the SSBCI program. Once the SSBCI Allocation Agreement is executed, U.S. Treasury will transfer the first tranche of funding to the State and the SBFC can begin deployment. The Allocation Agreement attached to the Resolution is a form document and the final version, when executed, will be substantially similar to the attached specimen document.

#### **ANALYSIS:**

Since the adoption of the Directives and Requirements in May 2015, and with subsequent Amended and Restated versions, dated October 24, 2017, and August 26, 2020, IBank and the Corporations have recognized some inconsistencies, obsolescence, and omissions that, have caused confusion. We have been creating a running list of this issues and are addressing them now because of the upcoming implementation of SSBCI 2.0.

The most notable proposed revisions are as follows:

- Maximum loan guarantee increase: Staff proposes increasing the maximum loan guarantee from the current \$2.5 million to \$5 million. The rationale for the increase is driven by the scale of SSBCI 2.0, through which IBank plans to allocate approximately \$391 million of new funds. U.S. Treasury has designed aggressive deployment targets for the program; SSBCI 2.0 allocations will be deployed in tranches of one-third each, and recipients need to deploy at least 80% of their current

tranche within three years in order to receive the subsequent one. The proposed increase is supported by prospective pipeline information from the Corporations indicating healthy demand for a larger guarantee, as well as the SBLGP's strong performance track record. The increased maximum guarantee would also support IBank's SSBCI strategies for expanding credit access to disadvantaged communities, a top priority of the program.

- Jump Start Loan eligibility changes: In an effort to add flexibility to the Jump Start Loan program, Staff proposes adjusting borrower eligibility to be based on either the low-wealth status of the borrower or the location of the business to be financed, rather than requiring that both the borrower and the business location meet low-wealth criteria. Staff also proposes the location component of the criteria ("Low-Wealth Community") be revised to be based on CDFI Investment Areas ("CDFI IA"s, as defined by federal code) rather than county-level per capita income data maintained by the State Employment Development Department ("EDD"). Besides being incorporated into the SSBCI 2.0 criteria for serving disadvantaged communities, CDFI IA eligibility can be easily confirmed through a user-friendly database maintained by the federal CDFI Fund.

In addition to the items above the following are recommendations for the most significant changes to the A&R Directives and Requirements. Changes not specifically addressed below are technical, non-substantive changes meant to enhance clarity for program stakeholders. However, all changes to the Directives and Requirements are reflected in attached Exhibit A (Clean A&R Directives and Requirements) and Exhibit B (Redline of A&R Directives and Requirements). Staff proposes that the changes to the A&R Directives and Requirements be implemented immediately upon Board approval. The one exception is that the proposed maximum Loan Guarantee increase not be considered effective until the Small Business Finance Center Manager provides a written certification that SSBCI 2.0 funds are available for deployment within the appropriate program accounts.

#### **PROPOSED CHANGES TO THE DIRECTIVES AND REQUIREMENTS:**

1. The A&R Directives and Requirements have been reformatted. For ease of understanding and program administration, staff proposes to add an index at the beginning of the document that shows the title of each section.

#### **§ 5000 DEFINITIONS**

2. **"Borrower"**

Staff proposes to change the definition of "small business." A section in the original definition referred to a code SBA uses to determine business size (not 750 or fewer employees). The section has been changed to state that a borrower is a small business with 750 or fewer employees.

3. **"CDFI Investment Area"**

Staff proposes to add the defined term "CDFI Investment Area" and to use the CDFI Investment Area/Low-Wealth Borrower definition to determine eligibility for the Jump Start Program.

4. **"Disaster Relief Borrower"**

Staff proposes to revise this definition consistent with the proposed revisions to the definition of Borrower described above.

5. **"Encumbrance"**

Staff proposes to add language to clarify how the encumbrance is calculated.

6. **"Farm Borrower Loan"**

Staff proposes to add language to clarify the outstanding dollar amount of a farm borrower

loan.

7. **“Farm Lender Credit Agreement”**  
Staff proposes to change the term “approved” to “executed.”
8. **“Guarantee”**  
Staff proposes to add language to clarify how a payment on a guarantee is calculated.
9. **“Jump Start Borrower”**  
Staff proposes to add the defined term “Low-Wealth Borrower” and use the CDFI Investment Area/Low-Wealth Borrower definition to determine borrower eligibility for the Jump Start Program.
10. **“Jump Start Corporation”**  
Staff proposes to update the name of the California Department of Business Oversight. The section has been changed to the California Department of Financial Protection and Innovation.
11. **“Loan Guarantee”**  
Staff proposes to add language to clarify how a guarantee is calculated.
12. **“Low-Wealth Borrower”**  
Staff proposes to add the defined term “Low-Wealth Borrower” and use the Low-Wealth Borrower/CDFI Investment Area definition to determine eligibility for the Jump Start Program.
13. **“Low-Wealth Community”**  
Staff proposes to revise the definition of “Low-Wealth Community” as one located in a CDFI Investment Area, replacing the prior definition based on county per capita income compared to the State average.
14. **“Principal”**  
Staff proposes to revise this definition consistent with the proposed revisions to the definition of Borrower described above.
15. **“Term Loan”**  
Staff proposes to add language to clarify the payment structure of term loans by borrowers.

#### **§5002 LOAN GUARANTEE TERMS**

16. Staff proposes to increase the maximum guarantee amount for any business to \$5,000,000 in preparation for the State Small Business Credit Initiative allocation.

#### **§ 5006 ADDITIONAL CLARIFICATIONS**

17. Staff proposes to remove the section that discusses the suspension or termination of a Corporation’s trust fund account. The program now has one pooled trust fund for all Corporations and no longer has separate trust funds for each Corporation.

#### **§ 5021 SECONDARY MARKET FOR GUARANTEED LOANS**

18. Staff proposes to remove the Assignment Registration Form from this section – as no such form exists.

#### **§ 5022 JUMP START LOAN PROGRAM**

19. Staff proposes to expand the eligibility for the Jump Start Loan Program by requiring the small business to either a Low-Wealth Borrower or be located in a Low-Wealth Community.

**RECOMMENDATION:**

Staff recommends approval of the Resolution 22-10 in connection with the following Amended and Restated Directives and Requirements for the Small Business Finance Center programs, including the Small Business Loan Guarantee Programs, the Farm Loan Program, the Surety Bond Guarantee Program, the Secondary Market for Guaranteed Loans and the Jump Start Loan Program, all of which are programs under the Small Business Finance Center. As noted, the \$5 million maximum Loan Guarantee would not become effective until the SBFC manager certifies receipt of SSBCI 2.0 funds.

Exhibits

- A) Clean Amended and Restated Directives and Requirements
- B) Redline of Amended and Restated Directives and Requirements