Date of Hearing: April 13, 2015

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Matthew Dababneh, Chair
AB 1393 (Burke) – As Introduced February 27, 2015

SUBJECT: California Pollution Control Financing Authority

SUMMARY: Expands the ability of the California Pollution Control Financing Authority (CPCFA) to offer loan loss reserve and other credit enhancements beyond small businesses. Specifically, **this bill**:

1) Allows the CPCFA to participate in an alternative funding source program which could include implementing loan loss reserve programs to benefit any person, company, corporation, public agency, partnership, or firm engaged in activities in California that requires financing.

2) Permits the CPCFA to offer financial assistance to include grants, loans, and credit enhancements.

3) Makes other conforming changes.

EXISTING LAW:

1) Establishes the CPCFA with specified powers and duties. (Health and Safety Code, Sections 44500 et seq.)

2) Provides that it is the intent of the Legislature to ensure that the state, through the CPCFA, may make maximum, efficient use of capital access programs enacted by all federal and state agencies, as well as funding available from any governmental program whose goals may be advanced by providing funding to the Capital Access Loan Program (CalCAP).

    a) In furtherance of this intent, and notwithstanding any other provision of this article, when the contributions required pursuant to Health and Safety Code Section 44559.4 (read below) are entirely funded by a source other than the authority, the authority may, by regulation adopted pursuant to subdivision (b) of Section 44520, establish alternate provisions as necessary to enable the authority to participate in the alternative funding source program. (Health and Safety Code 44559.11)

3) Authorizes the CPCFA to establish loss reserve accounts for financial institutions to participate in the CalCAP which provides loans to qualifying small businesses. (Health and Safe Code, Section 44559.4)

4) Allows the CPCFA or any other agency implementing a small business or brownfield site financing assistance program pursuant to an interagency agreement with the CPCFA, may adopt regulations relating to small business or brownfield site financing as emergency regulations in accordance with Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code. (Health and Safety Code 44520)

5) Defines "loss reserve account" as an account in the State Treasury or any financial institution that is established and maintained by the CPCFA for the benefit of a financial institution participating in CalCAP for the purposes of the following: (Health and Safety Code, 44559.1)

    a) Depositing all required fees paid by the participating financial institution and the qualified business;

    b) Depositing contributions made by the state and, if applicable, the federal government or other sources; and,

    c) Covering losses on enrolled qualified loans sustained by the participating financial institution by disbursing funds accumulated in the loss reserve account.

FISCAL EFFECT: Unknown.

COMMENTS:

The CPCFA has been providing low-cost innovative financing to California businesses since 1972. As a "conduit issuer" of tax-exempt private activity bonds, CPCFA is able to facilitate low cost financing to qualified waste and recycling projects. Other projects to control pollution and improve water supply can qualify for tax-exempt financing as allowed by federal tax law. Examples of recent assistance include projects to purchase clean-air vehicles by waste companies, construct and operate anaerobic digesters, recycle used oil, convert animal waste to clean burning fuel, and develop construction and demolition debris recycling programs.

In addition, CPCFA administers CalCAP which helps participating financial institutions extend credit to small businesses through microloans and larger loans for start-up, expansion and working capital up to $20 million. CalCAP was established through legislation in 1994 (AB 253, Bronshvag).

The CalCAP loan loss reserve program established through AB 253 was principally funded from the CPCFA's own revenues from fees collected on its bond issuances, and the statute set forth eligibility criteria for qualified lenders, borrowers and loan purposes. In addition, as part of the CalCAP statute, CPCFA has the ability to modify the program structure and criteria if the funds are from a source entirely other than CPCFA's own monies, known as an Independent Contributor. The regulations implementing the Independent Contributor permit the funding entity, which can be a public or private entity, to set program standards and modify the loan loss reserve criteria to further its policy objectives.

The Independent Contributor provisions have attracted federal and state agencies to CPCFA, to administer credit enhancement programs on their behalf. Examples include: $84 million allocated by the U.S. Treasury under the Federal State Small Business Credit Initiative: $54 million allocated by the Air Resources Board to fund the On-Road Heavy Duty Vehicle Air Quality Loan Program; $2 million (pending) allocated from the Energy Commission to establish the Electric Vehicle Charging Station Financing Program; and several others. These programs are examples of the ability of CPCFA to provide credit enhancement programs to mobilize private capital in support of state policy goals.

Need for the Bill

According to the sponsor, the California State Treasurer, John Chiang, the CPCFA fields requests from state agencies to administer new alternative financing and credit enhancement programs to encourage growth in the business sector, provide economic relief, or to leverage private capital. In particular, CPCFA has received repeated requests to develop pilot programs to incentivize consumer loans to individuals and loans to public or quasi-public entities. In addition, CPCFA has been examining the potential for state agencies to utilize financing structures which are different than loan loss reserves, but without clear statutory authority, CPCFA is reluctant to pursue additional financing options.

The objective of AB 1393 is to provide clarity regarding CPCFA's authority to set up loan loss reserve programs for individual consumers, to permit joint powers authorities and other public entities to be the borrower or beneficiary of these programs, and to create credit enhancement programs that vary from the standard loan loss reserve structure.

In addition, the sponsor states, to maintain the success of CalCAP, it must broaden its offerings to target and expand its reach to help more people. By providing additional credit enhancements to not only businesses but also individual consumers, CalCAP can provide loans to those that need help the most, whether that is rural farmers that need new wells for drought relief, or low income communities that could benefit from clean efficient cars.

CalCAP

As of March 31, 2014:

Total Number Loans Enrolled Over Program Lifetime:
17,202

For the Period: 1/1/14 — 3/1/14: Total Loans All Programs
908 loans for $55,385,429

Micro-Loans Enrolled (Loans under $40,000)
438 loans for $8,084,947

Average CalCAP Loan Amount
$60,998

CalCAP Small Business Program Loans
285 loans for $10,774,213

CalCAP Collateral Support Program Loans
6 loans for $5,950,000

CalCAP encourages banks and other financial institutions to make loans to small businesses that have difficulty obtaining financing. CalCAP is a form of loan portfolio insurance which may provide up to 100% coverage on certain loan defaults. By participating in CalCAP, lenders have available to them a proven financing mechanism to meet the financing needs of California's small businesses.

Program Flexibility

CalCAP offers lenders a mechanism to provide loans to small businesses that have difficulty obtaining financing. With CalCAP portfolio insurance, a lender is able to cover portions of loans that exceed the risk threshold normally set for business loans. The Program allows:

- Almost any small business loan, with a few exceptions.
- Insurance on a lender's portfolio of loans. Funds are placed in the loss reserve account as each CalCAP loan is enrolled.
- A Lender to enroll all or a portion of a loan, enabling a lender to cover loans beyond its conventional risk threshold whether it is for the entire loan or only a portion.
- Lenders to restructure loans by extending the terms of CalCAP loans, amending covenants or releasing collateral.
- Lenders to enroll up $2.5 million for loans as large as $5 million.
- A maximum lender/borrower contribution for any single borrower in a three year period of $100,000.

Eligible Uses of Loan Proceeds

CalCAP insures loans made to small businesses to assist them in growing their business. 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 limitations on real estate loans and loan refinancing.

Ineligible Uses of Loan Proceeds

CalCAP prohibits financing certain projects. Examples of ineligible uses of loan proceeds include gambling facilities, bars and adult entertainment businesses.

Terms

The maximum loan amount is $5 million and the maximum enrolled amount is $2.5 million. Each individual borrower is limited to a maximum $2.5 million enrolled over a 3 year period. Lenders set all the terms and conditions of the loans and decide which loans to enroll into CalCAP. Lenders determine the premium levels to be paid by the borrower and lender (within the parameters of the Program). Loans can be short- or long-term, have fixed or variable rates, be secured or unsecured, and bear any type of amortization schedule.

Eligible Lenders

Any federal or state-chartered bank, savings association, certified Community Development Financial Institutions (CDFI), or credit union is eligible to participate in CalCAP. A lender must certify that it is in good standing with its regulatory body (Federal Reserve, Federal Deposit Insurance Corporation (FDIC), Comptroller of Currency, Thrift Supervision, National Credit Union Administration (NCUA), or state banking authority). Other lenders, such as micro business lenders and finance companies may also be eligible.

How the Program Works

When a lender's first loan is enrolled, CalCAP establishes a loss reserve account for that lender. Each time a loan is enrolled under CalCAP, premiums are paid into the loss reserve account and CalCAP matches the premiums. For instance, if the lender and borrower each pay a 2% premium, CalCAP will typically pay 4%. For this one loan a total of 8% is added to the lender's loss reserve account for its entire CalCAP portfolio.

Loan enrollment applications must be received at CalCAP within 15 business days of the "Date of First Disbursement" (Date of Loan).

Businesses with addresses in High Unemployment Areas or Enterprise Zones are located within a Severely Affected Community (SAC). If the loan enrollment is for a business located within a SAC it may qualify for an additional premium equal to the amount of the lender premium.

The more loans a lender makes, the more dollars are deposited into the loss reserve account for its CalCAP portfolio.

How the Loss Reserve Account Grows

Over time, as more loans are enrolled, a loss reserve account grows, providing up to 17.5% (with addition of SAC premium) loss coverage on a portfolio of loans. For example, if a lender makes 10 loans totaling $500,000, the lender may have as much as $60,000 in its loss reserve account (using an average premium of 3% each from the lender and borrower, 6% from the Authority). If one loan of $50,000 defaults, the lender has immediate coverage of 100% of the loss. The lender must return recoveries from the borrower, less expenses, to the loss reserve account.

Eligible Small Businesses

- The borrower's business must be in one of the industries listed in the qualified Standard Industry Classification (SIC) or the North American Industry Classification System (NAICS) codes list.
- The borrower's primary business and at least 51% of its employees or business income, sales or payroll must be in California.
- The business activity resulting from the bank's loan must be created and retained in California.
- The small business must be classified as a small business under U.S. Small Business Administration guidelines (Title 13 of the Code of Federal Regulations) and have fewer than 500 employees.

Previous Legislation

AB 2749 (JEDE), Chapter 132, Statutes of 2014 made various technical changes.

AB 850 (Nazarian) Chapter 636, Statutes of 2013 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 CPCFA.

AB 981 (Hueso), Chapter 484, Statutes of 2011 provided additional incentives within CalCAP to encourage lenders to lend to small businesses.

AB 1632 (Blumenfield), Chapter 731, Statutes of 2010, specifies that severely affected communities includes areas with unemployment above 110 % of the statewide average for purposes of expending allocated funds. Also allows CalCAP to establish regulations necessary for participation in programs associated with funds from other sources.

SB 1311 (Simitian), Chapter 401, Statutes of 2008, permits CalCAP to contribute an equal amount to an enrolled loan's loss reserve account as the lender, and to withdraw all accrued interest from enrolled loss reserve accounts to assist with administrative cost.

SB 1119 (Alarcon), Chapter 756, Statutes of 1999, authorized CPCFA to issue revenue bonds to assist responsible parties pay their liability toward the clean-up of federal Superfund sites. It also made other changes to improve small businesses' access to capital under CPCFA's program.

AB 253 (Bronshvag), Chapter 1163, Statutes of 1994, expanded the CalCAP program to all small businesses instead of only those industries with operations that adversely affected the environment. Also, it provided greater risk coverage for loans made to small businesses located in geographic areas affected by military base closures or aerospace downsizing.

Double Referral

This measure is double-referred to the Assembly Committee on Jobs, Economic Development and the Economy.

REGISTERED SUPPORT / OPPOSITION:

Support

California State Treasurer (Sponsor)

Opposition

None on file.

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