BEST PRACTICES FROM PARTICIPATING STATES:
CAPITAL ACCESS PROGRAMS

SEPTEMBER 2015

SSBCI

Acknowledgements

This SSBCI Best Practices document resulted from many constructive discussions of the CAP Working Group. SSBCI thanks the following members of the working group for their time and thought leadership in support of this project:

- Chris Cook, Director, Capital Access, Michigan Economic Development Corporation
- Jillian Franzoia, CalCAP Manager, California Pollution Control Financing Authority
- Sherri Martin, Development Representative Supervisor, Florida Department of Economic Opportunity
- Jennifer Schrader, Development Representative, Florida Department of Economic Opportunity
- Jane Swanson, SSBCI Program Manager, Washington State Department of Commerce
- Matt Tuohy, Program Manager, Indiana Economic Development Corporation
- Thomas Wall, Director, North Carolina Rural Economic Development Center

SSBCI also thanks Ron Kelly from the Center of Regional Economic Competitiveness for facilitating the working group sessions and collecting perspectives. We also wish to thank Zakaria Shaikh at the Department of the Treasury for his assistance in producing this document.

Jeffrey Stout
Director
State Small Business Credit Initiative

State Small Business Credit Initiative
Capital Access Program Best Practices

Under the U.S. Treasury's State Small Business Credit Initiative (SSBCI), 24 states[1] allocated a portion of their funding to Capital Access Programs (CAPs). State-funded CAPs existed in many states before SSBCI. Initially, states allocated $291 million in SSBCI funds to CAPs, but CAPs were unable to attract the level of interest they originally anticipated from financial institution lenders. As of June 2015, states shifted about 84 percent of that allocation to other SSBCI programs, leaving $46 million allocated to CAPs. To strengthen the states' performance in these programs and to assist states considering the creation of a CAP, a working group of state officials who have operated CAPs met to discuss their experiences and common practices. This document distills the most important and practical advice CAP state managers would offer their peers.

In an SSBCI CAP, the state sets up a reserve account at each lender to cover losses on enrolled loans. Both the lender and borrower contribute a percentage of an individual loan or line of credit to the reserve fund for a total of 2 to 7 percent of the loan amount. The state then matches these contributions to the reserve account dollar-for-dollar using SSBCI funds. Lenders may use the reserve account to cover any losses on their CAP loans.

States with a variety of implementation experiences participated in the CAP Working Group including those with newer and more established programs, and programs with large and small allocations. The CAP Working Group discussed and agreed upon successful practices that could be readily implemented by other states. The working group agreed that the following five key principles apply to all CAPs:

1) **Identify a key senior executive at a lender and a key senior official at the state implementing agency who will be champions for the program.**

2) **Make sure CAP staff acquires the appropriate compliance experience or training.**

3) **Design the program to be easily used by lenders.**

4) **Solicit feedback from multiple lenders during the design phase.**

5) **Think strategically about how the CAP will be funded, either by public or private sources, in the future.**

In the sections that follow, we present observations and successful practices in the areas of program design, marketing, operations, monitoring and evaluation, sustainability, and defaults and collections.

[1] "State" includes states, territories, the District of Columbia, and municipalities approved to participate in SSBCI.

1. Program Design

- **Solicit feedback from lenders during the design phase:** Feedback from lenders will help address lenders' concerns upfront so they will be more likely to utilize the program. The early engagement of lenders also bolsters their buy-in before the CAP is implemented. However, such engagement and early interest does not always turn into usage. Some states found that multi-state lenders were initially interested in CAPs; however, these lenders did not participate due to the challenges of standardizing CAPs across states. Another challenge for states with established CAPs was that some of the regulations associated with the SSBCI CAP were different from existing state-supported CAPs. In these situations, some states found it difficult to sell the "different" SSBCI CAP.

- **Focus on enrolling regional and community lenders, including micro-lenders and Community Development Financial Institutions (CDFIs):** Regional and community lenders are more likely to use CAPs. One reason for this is that the program is geared toward smaller transactions. Unlike multi-state banks, which are often dissuaded from using the program due to their centralized underwriting procedures, micro-lenders and CDFIs have been ardent users of CAPs in many states. Some states have viewed these high usage rates as an opportunity to tailor their programs around the needs of such lenders.

- **Assure lenders that the state is committed to the CAP's sustainability:** If lenders are under the impression that CAP funding will run out in a few years or will be inconsistent over time, they will be less likely to adopt the program. Some lenders have asked for the state's commitment to future funding and an assurance of program longevity. Some states found support from high level state officials who spoke to lenders and banking associations to help alleviate lenders' concerns.

- **Identify the senior lending executive and senior state official who can serve as champions for the program:** Support from executives and officials is important during the design and marketing phases of the CAP. The senior lending executive should be willing to recommend the CAP to other financial institution lenders with the end goal of program growth.

- **Use incentives to help give lenders peace of mind by enabling their reserve accounts to grow:** Incentives encourage lenders to make their initial loans and subsequently see their reserve accounts grow. Incentives that some states offer include direct state subsidies to reserve accounts for lenders enrolling loans to borrowers in specific target areas, *e.g.,* those in low-to-moderate income areas, or to minority- and veteran-owned businesses.

- **Design an informational document that lenders can provide to prospective borrowers:** This document should be a two-page form letter lenders can provide to borrowers that clearly explains the CAP fee structure. This will help lenders facilitate the enrollment of CAP loans.

- **Keep CAPs simple and user friendly for all lenders:** Successful CAPs have a simple loan enrollment form and do not require states to underwrite loans. For simplicity, states should focus on determining the eligibility of loans for enrollment to confirm that loans meet program criteria.

2. Operations

- **Build and maintain positive relationships with lenders:** States have found that building relationships with lenders is one of the best ways to encourage usage of the program. It is important for states to maintain these relationships by meeting with loan officers. For example, New York's Empire State Development (ESD) used the trust it had built and maintained with lenders through its other small business loan programs to gain support for its CAP.

- **Focus on customer service provided to the lender:** Successful programs are customer-focused and include quick response times to lenders' questions and quick loan enrollment. For example, California's CAP (CalCAP) has implemented customer-focused practices such as answering all questions from lenders within a specific time frame.

- **Establish agreements with lenders:** Lender agreements open a dialogue with the lender, set expectations for the program, and initiate the process of setting up reserve accounts. For example, Indiana Economic Development Corporation (IEDC) has a lender participation agreement that clearly sets forth the guidelines for setting up reserve accounts, enrolling loans, and reporting. Additionally, the agreement includes guidelines regarding specific loan enrollment questions such as refinancing loans, increasing loan amounts, and handling lines of credit. IEDC has also provided lenders with a borrower disclosure document.

- **Implement electronic loan enrollment and develop concise documentation:** Many lenders prefer electronic loan enrollment. This allows lenders to upload loan enrollment documents into their loan administration systems, automatically input loan information, and develop streamlined documents such as a one-page loan enrollment form. States have also found it is important to make the documentation concise.

- **Plan for staff succession:** Always assume that the program's existing staff may change. Develop operation manuals and policies that address tasks and processes and keep them up-to-date. Develop checklists for key operational activities, such as loan approvals, enrollment, collections, reporting, and compliance. Similarly, each staff member should identify his or her primary responsibilities and commit them to writing.

3. Marketing

- **Develop a one-page brochure or fact sheet for lenders as a reference and marketing tool:** This document can help start conversations with lenders and should include a broad overview of the CAP. The fact sheet should also include loan enrollment steps.

- **Recognize that the CAP website is important to lenders, and make sure it is current, easy to find (remember the "3-click" rule), and has all the pertinent information:** The website should be a reference point for lenders and prospective borrowers. Although a web presence for the CAP is important, it should not be seen as the primary method to market the program. Oftentimes, the website serves as a companion to a brochure; it explains the program and includes contact information. Some states include success stories, while others include links to forms.

- **Perform initial outreach to the loan officers and then to key decision makers:** Loan officers will often be the first point of contact when marketing a program, but it is vital to find a high-level champion for the CAP within a lending institution. Loan officers will inquire about the specifics of the program and ease of use, while management will usually weigh the benefits and drawbacks for the lender. Having a directive from management to utilize the program will lead to more engaged relationships with loan officers.

- **Review the enrollment process with lenders (including loan officers and executives) while marketing the program:** This review process helps build relationships with lenders and provides an opportunity to address any questions or concerns.

- **Use compliance visits to build relationships and answer general questions:** Some states use compliance visits to fulfill multiple purposes beyond general compliance auditing. CalCAP uses compliance site visits as an opportunity to make face-to-face contact with lenders and develop trust. Additionally, CalCAP uses compliance visits to provide training sessions for lenders who have new staff or want refresher training.

4. Monitoring and Evaluation

- **Reconcile all reserve accounts periodically:** Reconciling reserve accounts allows program managers to proactively detect and correct any funding errors.

- **Review the state's procedures against the SSBCI National Standards for Compliance and Oversight to adhere to the program requirements:** It is critical to stay current with program rules.

- **Make lenders and borrowers aware of certification and assurance requirements and monitor their compliance:** Borrower and lender certifications and use of proceeds assurances help monitor compliance on the front end and inform parties of the requirements. With CAPs, most of the program monitoring happens upfront, so it is important to have enrollment forms that reflect the certification and assurance requirements.

- **Train CAP staff on compliance with program rules:** States have hired individuals with U.S. Small Business Administration loan experience, experts in bank documentation, paralegals, and other experienced professionals to build a rigorous compliance regimen. Staff should also have good interpersonal skills to allow them to build relationships with lenders that will be crucial to CAP success.

- **Create a compliance checklist and use it prior to enrolling each CAP loan:** A checklist informs the program administrators and the lenders of what is expected.

- **Notify participants of program changes by updating documents and website, and proactively communicating changes to lenders:** Timely communication with lenders regarding program changes is important. States should explain to lenders how program changes will affect CAP procedures.

- **Solicit feedback from lenders:** It is important to find out what is working and what may need to be adjusted in program design or operations.

- **Attach a confidentiality agreement to the approval document to address concerns about Freedom of Information Act (FOIA) and other public disclosure requirements:** It is important to make lenders aware of disclosure requirements. CalCAP uses a privacy notice that lenders are required to give to each borrower who will be enrolled in the program. The lender verifies on the lender certification submitted with the loan enrollment application that the borrower was provided with the notice. The borrower verifies that they received the privacy notice on the borrower certification submitted with each loan enrollment application. CalCAP's notice is available on its website, allowing lenders to easily access the document.

- **Proactively prepare CAP data for stakeholders:** Some stakeholders are more interested in a program's job creation and cost efficiency than private sector matching funds. Some states proactively produce a brief document for policymakers with key data points of interest. It is a good practice to periodically update this document with the latest data. Michigan Economic Development Corporation (MEDC) prepares a report for the legislature each year that includes all MEDC-supported projects. Using CAP data, MEDC can demonstrate that it is supporting large companies as well as smaller "Mom & Pop" operations.

5. Sustainability

- **Include a CAP as part of a menu of small business loan programs to increase the likelihood that the CAP will be used and sustained:** As a result of deal flow and relationships from loan participation and other programs, states can position CAP as a niche product to be used by lenders as needed.

- **Consider recycling program income from other SSBCI loan programs into CAP:** Relative to other program types, CAP needs less funding for its survival. One way to maintain funding for CAP is through income from other programs.

- **Pay attention to old reserve accounts:** Identify reserve accounts that have been inactive for a certain amount of time, *e.g.*, three years or more, and attempt to re-activate the accounts or recoup the funding. Recouping funds might not always be a good idea. Leaving funds in reserve accounts can entice lenders to utilize the CAP, and is in keeping with the promise to lenders upon entering the program that the reserve funding will be reliable. Many states consider funds set aside in CAP reserve accounts to be irrecoverable.

- **Understand that CAPs promote access to capital but do not generate a return on investment:** Funds allocated to CAPs are considered "spent money" by many states. Over the long term, CAPs require a continued funding stream to maintain operations.

6. Defaults and Collections

- **Develop processes to monitor dormant reserve accounts:** States have databases to track loans, but oftentimes do not have a formal process set up at the beginning of the program to manage inactive accounts. If the lenders do not intend to use program and there is language in the lender agreement that allows recoupment of reserve account funds, the state may want to find a means to use those funds. In developing a new SSBCI agreement, one state added term limits to loans to prevent funds from remaining in dormant accounts.