New York City Council
Hon. Christine C. Quinn, Speaker
Hon. Domenic M. Recchia Jr.
Hon. Diana Reyna

Finance Division
Preston Niblack, Director
Jeffrey Rodus, First Deputy Director

Small Business Credit Summit

April 20, 2010

Raymond Majewski, Deputy Director/Chief Economist

Jan Messerschmidt, Policy Analyst

Ralph P. Hernandez, Legislative Financial Analyst

Paul Sturm, Supervising Legislative Financial Analyst

Zaid Sadoun, Legislative Financial Analyst

Emre Edev, Senior Legislative Financial Analyst

"Large companies have got lots of money, lots of liquidity and complete access to markets"

Jamie Dimon, CEO at JP Morgan Chase

Introduction

Small business is in trouble. There is evidence that small firms have been hurt by this recession to a greater extent than larger firms, and that small firms have been less able to benefit from the recovery. According to the Federal Reserve Bank of Atlanta, 45 percent of total job loss in the first part of what is now being called "The Great Recession" came from small firms. This is very different from the previous recession in 2001 when just 9 percent of job losses were from small firms. However, it is similar to the recession of 1990-1992 when small business lost 43 percent of the jobs. [1] [2] One of the things that the Great Recession and the recession of 1990-1992 have in common is that both were associated with credit crunch problems in the banking system.[3] The recession of 2001 did not entail similar credit problems.

The crisis squeezed banks, which in response reduced their lending. Small businesses are vulnerable in this environment. The general contraction of credit badly affected small businesses, in particular those in the City. The National Federation of Independent Business surveyed small businesses in the late fall of 2009. They found that during the recession there had been a significant decrease in the percentage of firms whose credit needs were being met. Even among those who did get credit, about 20 percent either had complaints over terms and conditions or actually rejected loans because of the difficult terms and conditions.[4]

This paper looks at the impact of the credit crisis on banking, small business finance and the conditions small businesses face in New York City. It also reviews government and private sector responses to the crisis. The last section considers gaps in the response to the crisis and whether there are opportunities for public/private partnerships in closing some of those gaps.

---

[1] Federal Reserve Bank of Atlanta Macro Blog http://macroblog.typepad.com/macroblog/2009/10/prospects-for-a-small-business-fueled-employment-recovery.html Thanks to Aysegul Sahin of the Federal Reserve Bank of New York for bring this to our attention and helping us understand the difficulties faced by small firms during the great recession.

[2] Data on small business will be a problem throughout this white paper. The FRB Atlanta numbers cited in footnote 1 are from Bureau of Labor Statistics Business Employment Dynamics, whose most recent data is from 2008Q4. The only reasonably complete data set for studying small business finance, the Federal Reserve Survey of Small Business Finance, has not been updated since 2003. Data at the New York City level is even less complete and arrives with even longer lags.

[3] For small business and the recession of 1990-92 see Allen Berger & Gergory Udell, "The Economics of Small Business Finance: The Roles of Private Equity and Debt markets in the Financial Growth Cycle" Journal of Banking and Finance, Vol 22, 1998.

[4] William Dennis Jr. "Small Business Access to Credit in a Deep Recession" presentation to the National Association of Business Economists, Small Business Roundtable, March 23, 2010.

The Banking Sector Crisis of 2008: Background

General Description of the Crisis

The Great Recession had its roots in 2006, when aggressively sold subprime mortgages started to default, causing the numerous securities they had been packaged into to default as well. What had been previously viewed as reliable investment vehicles quickly became viewed as 'toxic assets' and began to drag down balance sheets everywhere.

Investment banks, particularly Bear Stearns and Lehman Brothers, were highly exposed. The impact on balance sheets was so great that by early 2008 investors did not want to provide the short-term loans that investment banks use for funding. Markets had lost their faith in the banks' ability to repay their debt. Interest spreads shot up and investors flocked to Treasuries.

Bear Sterns' forced sale to JPMorgan Chase in March did not inspire confidence, and when Lehman Brothers filed for bankruptcy in September of 2008, a full scale financial panic erupted. After all, if the storied Lehman Brothers could fail, who was safe?

Financial markets effectively froze, cutting off even healthy businesses from credit. Non-financial firms and households suffered from the general lack of credit, due to the paralysis of both the banks and capital markets.

Impact of the Crisis on Commercial Banks and Thrifts

The crisis shifted the focus of investment banks from finance to self-preservation. Governments around the world eased monetary policy and injected billions of dollars into financial markets and investment banks. This was done to shore up balance sheets and generally stem mounting losses in asset value, liquidity and confidence. These policies helped restore investment banks to profitability by 2009,[5] allowing them to repair their balance sheets and resume their role as financiers.

Losses at deposit-taking commercial banks, on the other hand, continued to mount through 2009. Of the 8,012 commercial banks and thrifts insured under the Federal Deposit Insurance Corporation (FDIC), 29.5 percent lost money—well above the single-digit figures of the middle of the decade. From 2003 through 2007 only 10 such institutions had failed. By contrast in 2008 this figure was 25, while 2009 saw 140 failures. This year commercial banks, a key source of small business loans, continue to fail in significant numbers.

Consequently, lending by these deposit-taking institutions has plummeted. Although residential real estate lending and consumer lending started to stabilize in the third quarter 2009, commercial and industrial (C&I) lending and commercial real estate lending had yet to do so by the fourth quarter.[6] According to the Federal Reserve's Flow of Funds report, in 2009 C&I lending by commercial banks fell by around 24 percent. [7].

[5] New York Stock Exchange member firms' total profit was $61.4 billion in 2009, their highest ever. This followed losses of $42.6 billion in 2008, and $11.3 billion in 2007.

[6] FDIC Quarterly Banking Profile: Fourth Quarter 2009. 2010, Volume 4, Number 1.

[7] Counterintuitively, according to Elizabeth Duke, of the Board of Governors of the Federal Reserve, there was less business loan contraction in smaller banks, which tend to serve small businesses, than in larger banks. Banks with less than $10 billion in total assets reduced their business loans (including C&I and CRE) by an annualized 12.8 percent in the fourth quarter of 2009. Large bank, however, reduced their business loans by more than 20 percent

Changing Commercial Banks' and Thrifts' Attitudes towards Risk and Small Business Lending – The Supply Side of Credit

Part of the reason for the continued weakness in the small business loan market is the shrinking supply of credit available to it. This shows up most clearly in the banks underwriting standards. According to the July 2009 Survey of Credit Underwriting Practices by the Comptroller of the Currency, 64 percent of banks reported they had tightened their lending standards in the small business market. According to the more recent Federal Reserve Board's January 2010 Senior Loan Officer Opinion Survey of Bank Lending Practices, this continued in the second half of 2009. There is some evidence that this tightening is coming to and end and that we can anticipate somewhat more relaxed conditions over the year.

For small businesses this tightening of credit shows up in higher interest rates, smaller lines of credit, and rejected loan applications. According to the most recent NFIB survey, 21 percent of businesses that attempted to borrow received only some of the credit they wanted. Of those who had their loans continued, 42 percent reported an increase in interest rates on their credit lines and 52 percent on their credit cards.[8]

This tightening of credit standards reflects both a general change in attitude towards risk in the economy as a whole and some problems specific to the banking system. For a number of years before 2007 individuals and institutions were unusually willing to undertake risk in the financial system. In the bond market the premium paid by risky bonds was unusually low. In the housing market people were willing to buy houses with mortgage payments that stretched their income. In the derivative markets investors were willing to buy novel assets whose characteristics were not well understood. With the financial crisis all of this has changed and everyone has backed away from risk.

In addition for the banking system there is the issue of capital. For a bank the ability to accept deposits and make loans depends upon the bank having a capital reserve that can be set aside to cover losses on loans and other assets. By regulation and also by simple prudence, the amount of capital required depends upon the risk of the loans being made. Banks have suffered significant losses.[9] They also have increased their capital reserves for bad loans and other losses. Regulators may also be paying closer attention to these issues than they did in the recent past.[10] In addition, prior to 2007 it was possible for banks to package and sell off some of their loans, effectively taking them off their books. Since the crisis, this secondary market for loans has closed to all but federally backed loans. As a result, banks have less capability to take on risk than they did in the past.

Compounding this issue is that lending to small business has grown riskier. Commercial and industrial loans are a good proxy for measuring small business loan activity. According to the Federal Deposit Insurance Corporation (FDIC), C&I loan payments that are over 90 days past due rose from around 0.7 percent in the quarters leading up the crisis to 3.1 percent in the fourth quarter of 2009.[11] Banks also

[8] 'Small Business Access to Credit in a Deep Recession.' William J. Dennis, Jr., National Federation of Independent Businesses, March 2010.
[9] FDIC "Quarterly Income and Expenses of FDIC Insured Banks and Savings Institutions"
[10] See "Testimony of Stephen G. Andrews on behalf of the Independent Community Bankers of America" before the House of Representatives Committee on Financial Services and Committee on Small Businesses" February 26, 2010.
[11] Quarterly Loan Portfolio Performance Indicators, All FDIC-Insured Institutions

reported that the credit quality of their C&I loans to small firms were generally worse than to larger firms.[12]

An additional hurdle for small businesses is that they frequently use their real estate as collateral and the value of those assets has plummeted. According to the NFIB survey, 93 percent of small business owners own their own home, 50 percent own their business premises, and 39 percent own other real property.[13] These same businesses that previously received credit are often denied loans due to the reduced value of their collateral

It should be noted that in a recession it is common for the demand for loans to fall. In a shrinking economy there is less need to finance economic activity. This recession was no different. According to the Federal Reserve's Senior Loan Officer Opinion Survey, 34 percent of banks reported reduced demand for C&I loans, while only 9 percent reported increased demand.[14] This doesn't alter the fact that firms that are seeking credit are having greater difficulties obtaining that credit on terms they find acceptable.

Small Business Credit

The problem of small business credit

Providing credit to small business is very different from providing credit to large firms. There is a lot less information publically available about small firms. Large firms may be registered with the Securities and Exchange Commission, their activities may be reported in the press, and they have audited financial statements. This public information makes it easier to figure out the credit worthiness of large firms. Because of this, large firms often have many different ways of borrowing and many different sources of credit.

Small businesses are more opaque and they are fragile. It is estimated that 24 percent of small businesses disappear within two years and more than half disappear within 4 years.[15] It can take much work on the part of the owners of small firms to prove that they are credit worthy. Similarly it is more costly for lenders to screen and monitor small business, considering the lesser amounts of credit requested. This is a situation that favors financial intermediaries such as banks, though trade credit from suppliers and in some cases family and friends may also be available.

It is generally advantageous for a firm to establish a relationship with a financial institution that will provide multiple financial services including credit. These multiple services give the banks information advantage in monitoring the condition of the small business and the appropriateness of extending additional credit. There is empirical evidence that small firms that have strong relationships with

[12] Federal Reserve's Senior Loan Officer Opinion Survey on Bank Lending Practices, January, 2010.
[13] 'Small Business Access to Credit in a Deep Recession.' William J. Dennis, Jr., National Federation of Independent Businesses, March 2010.
[14] The Federal Reserve Board, "The January 2010 Senior Loan Officer Opinion Survey on Bank Lending Practices," http://www.federalreserve.gov/boarddocs/snloansurvey/201002/fullreport.pdf.
[15] Berger & Udell p. 12.

prospective lenders are more likely to receive credit and are likely to pay lower interest rates.[16] This means that it can be particularly difficult for a small business when the institution it has been dealing with finds itself no longer willing or able to extend credit. This is one of the issues currently faced by small business.

To quote the Comptroller of the Currency, "With the uncertainties banks have faced in the severe downturn and stressed financial markets, some may have become too conservative and denied credit to truly creditworthy borrowers." [17] But there is another dimension to this. Some financial institutions have fared better through the financial crisis than others. The ones that have done badly may need to take a more conservative position on risk than other institutions. If you are doing business with an institution that has been hurt, you may find yourself out of luck. Accessing credit from other institutions may be possible, but it is not simple.

Sources of Credit

Small businesses require credit to finance real estate, new investments, replacement of old equipment, inventory and general cash flow requirements, such as payroll. The overwhelming majority of small business, 89 percent, use some form of credit. The most important source of credit, by far, is commercial banks, followed by finance companies.

Table 1: Share of Aggregate Value of Small Business Debt by Source of Credit

Type of Creditor	Fraction
Credit union	0.5%
Thrift	6.3%
Commercial bank	57.5%
Finance company	15.9%
Brokerage	1.0%
Leasing	3.1%
Other Nondepository	7.2%
Family	3.0%
Other Businesses	1.4%
Government	3.5%
Other individual	0.2%
Not classified	0.1%
Total	**100%**

Source: Charles Ou & Victoria Williams, "Lending to Small Businesses by Financial Institutions in the United States" Small Business in Focus: Finance, Small Business Administration Office of Advocacy July 2009 -- based on FRB Small Business Finance Survey 2003.

[16] See the literature review in Rebel A. Cole, "Who Needs Credit and Who Gets Credit? Evidence form the Surveys of Small Business Finance, Small Business in Focus: Finance, Small Business Administration Office of Advocacy July 2009

[17] John C. Dugan, Comptroller of the Currency, "Testimony before the Committee on Financial Services and the Committee on Small Business" U.S. House of Representatives, February 26, 2010.

What kind of credit does small business use? The most common form is the credit card, followed by line of credit, vehicle loan and loan from the owner. The probability that credit will be used increases with the size of the business, and certain types of credit are more important for larger small businesses. This is especially true of lines of credit, obtained by only a small percentage of very small firms but used by the overwhelming majority of medium size firms.

Table 2: Share of Small Firms Using Credit by Credit Type

	Any Firm	**Firm by Employment Size**					
Loan Type		**0**	**1 - 4**	**4 - 9**	**10 - 19**	**20-99**	**100-499**
Any Credit	**89.0%**	**80.9%**	**89.9%**	**94.3%**	**96.5%**	**97.2%**	**97.7%**
Traditional Loans							
Line of Credit	**34.3%**	17.9%	32.5%	45.3%	49.5%	60.2%	82.5%
Mortgage	**13.3%**	6.8%	14.8%	15.4%	19.0%	20.9%	28.1%
Vehicle Loan	**25.5%**	17.2%	24.5%	31.7%	35.9%	36.3%	35.7%
Equipment Loan	**10.2%**	4.1%	6.2%	14.9%	20.2%	26.6%	32.4%
Lease	**8.7%**	4.4%	7.2%	12.3%	12.5%	17.7%	28.0%
Other	**10.1%**	7.2%	7.5%	14.1%	15.3%	16.0%	18.7%
Personal Credit Card	**46.7%**	49.6%	47.6%	47.1%	44.8%	34.3%	32.1%
Business Credit Card	**48.1%**	33.3%	50.1%	59.1%	58.3%	62.6%	71.7%
Owner Loan	**16.8%**	4.7%	17.0%	25.6%	27.4%	32.8%	27.8%

Source: Charles Ou & Victoria Williams, "Lending to Small Businesses by Financial Institutions in the United States" Small Business in Focus: Finance, Small Business Administration Office of Advocacy July 2009 -- based on FRB Small Business Finance Survey 2003.

How do small businesses access credit? From the table below, one can see that it is the owner, via the owner's business credit card, that is the most common source. After that come commercial banks and finance companies. Once again, the likelihood of using these institutions grows with the size of the firm.

Table 3: Share of Small Firms Using Credit by Credit Supplier

	Any Firm	**Firm by employment size**					
Lender		**0**	**1 - 4**	**5 - 9**	**10 - 19**	**20-99**	**100-499**
Depository institutions							
Credit union	3.9%	4.3%	3.2%	4.5%	3.3%	3.8%	2.2%
Thrift	5.5%	2.9%	6.0%	5.9%	8.7%	8.9%	8.2%
Commercial bank	41.0%	20.8%	39.4%	55.6%	61.1%	69.4%	65.7%
Nondepository institution							
Finance company	22.1%	14.2%	20.0%	29.0%	30.1%	36.2%	40.6%
Brokerage	0.7%	0.3%	0.4%	1.5%	1.0%	1.5%	2.8%
Leasing	4.2%	1.7%	3.8%	5.5%	7.8%	8.1%	1.4%
Other	1.1%	0.9%	0.8%	2.2%	0.7%	0.7%	0.7%
Non Financial							
Family & friends	6.2%	4.4%	5.3%	8.2%	10.0%	6.7%	10.6%
Other businesses	2.6%	2.4%	1.6%	3.7%	4.0%	3.0%	4.3%
Government	1.3%	0.9%	0.5%	1.8%	2.4%	3.1%	5.7%
Other	0.4%	0.5%	0.2%	0.7%	0.0%	0.7%	0.2%
Other							
Owner loans	1.7%	4.7%	17.0%	25.6%	27.4%	32.8%	27.8%
Owner credit card	46.7%	49.6%	47.6%	47.1%	44.8%	34.3%	32.1%

Source: Charles Ou & Victoria Williams, "Lending to Small Businesses by Financial Institutions in the United States" Small Business in Focus: Finance, Small Business Administration Office of Advocacy July 2009 -- based on FRB Small Business Finance Survey 2003.

Impact of the crisis on small businesses in New York City

The State's Economic Development Law defines small businesses as employing up to 100 persons, independently owned and operated, and not dominant in their sector.[18] Roughly 98 percent of New York City firms have fewer than 100 employees, and 94 percent have less than 50.[19] An estimated 51 percent of private jobs in the City are provided by firms with less than 100 employees, while around 39 percent of positions are in businesses with fewer than 50 workers.[20]

If we use the 50 or less definition for small business, the City sectors in which over 50 percent of employees work in small businesses include (from highest concentration down) real estate, building construction, food & drinking services, retail, wholesale and manufacturing.

National data cited earlier indicate that small businesses have especially suffered from the recession. Turning to the City, the Finance Division of the New York City Council compared employment concentration in small business with job loss during the recession for each sector.[21] While no across-the-board relationship was established, there were sectors with high small business concentration that especially suffered since August 2008.[22] The building construction and manufacturing sectors suffered particularly severe contractions (see Table 4). For construction this was a result of its fortunes being tied to the now stagnant real estate development in the City. The manufacturing sector, on the other hand, has been structurally downsizing for many years, due to the especially high cost of locating in the City. At the other end of the spectrum, food services and drinking places have held up relatively well over the past 18 months, as relatively buoyant tourism has helped to buffer this sector.

---

[18] New York State Economic Development Law § 131.
[19] County Business Patterns, 2007, U.S. Census Bureau
[20] Id.
[21] Data limitations required our using entire City sectors with high small business employment, instead of direct data from the small businesses, which is not readily available.
[22] Current Employment Survey, NYS Department of Labor, February 2010, County Business Patterns 2007. U.S. Census Bureau

Table 4: Sectors with a Majority of Their Jobs in Small Businesses

Sector	Jobs in Small Businesses	% Change in Emp. since Aug 2008	Change in Emp. since Aug 2008	Total Emp. Feb 2010
Real Estate and Rental & Leasing	66.9%	-3.8%	-4,700	119,100
Construction of Buildings	62.3%	-17.6%	-6,500	30,500
Food Services and Drinking Places	59.3%	-1.3%	-2,500	196,200
Retail Trade	56.6%	-5.0%	-15,100	285,000
Wholesale Trade	55.6%	-9.1%	-13,600	135,300
Manufacturing	51.7%	-14.5%	-13,600	79,900

Source: New York State Department of Labor

With a national recovery at hand, the City remains in a deep small business recession. One of the chief symptoms is that businesses are not accessing credit. Businesses require credit to expand their operations and to finance payroll and inventory. With prospects of sustained consumer activity still tentative, the small business loan applications that are occurring are more focused on maintaining operations than on expansion.

In New York and other large cities small businesses are especially dependent on large banks, due to the dominance of mega banks, and their superior lending capacity. Unfortunately, borrowing from large banks has become considerably more impersonal in the City. Loan applications are no longer being comprehensively evaluated locally in underwriting departments, with which small businesses developed a personalized relationship over the years. Centralization of underwriting has resulted in an increasing focus on credit scores and similar metrics. As part of the tightening of credit standards discussed above, these threshold requirements have been significantly increased. Before the financial crisis small businesses could usually obtain loans with scores in the upper 600s; loan applications are now being rejected with scores as high as the mid and upper 700s. Consequently, borrowers in the City who have received credit for years are now seeing their credit lines withdrawn or severely reduced with more stringent terms.

Banks are understandably concerned about risk and do not want to make more high-risk loans. Many small businesses are also not ready to take on loans to expand or even replenish their inventory until the economic recovery gains a firmer foothold in the City.

Responses

A. Government responses/programs

Federal

In response to the credit crisis, the U.S. Small Business Administration (SBA) has launched different incentives for lenders and borrowers to get credit flowing again for small businesses including:[23]

- *Eliminating and reducing fees for borrowers on 7(a) loans and for borrowers and lenders on 504 loans:* The SBA's 7(a) program assists qualifying small-business borrowers by providing loan guarantees, limiting the lenders' losses in the event that a borrower defaults. The guarantee covers 50 percent to 85 percent of a loan's balance, thus putting the credit risk of the loan to the federal government. [24] The SBA 504 Loan Program would include: a loan secured from a private sector lender with a senior lien covering up to 50 percent of the project cost; a loan secured from a Certified Development Company (CDC) (backed by a 100 percent SBA-guaranteed debenture) with a junior lien covering up to 40 percent of the total cost; and the contribution from the borrower of at least 10 percent equity.[25] SBA eliminated the upfront borrower's fees for both the 7(a) and 504 loan programs.[26] The fee reductions can free up capital that small businesses can use elsewhere for their business. According to SBA, the temporary fee eliminations for 7(a) loans would support an overall program level of $8.7 billion, while the 504 loans fee elimination would support $3.6 billion.[27]

- *Raising the guarantee on 7(a) loans from 75 or 85 percent depending on the size of loan to 90 percent:* in addition to the fee eliminations from 7(a) loans, SBA also increased the loan guarantees, thus, mitigating the banks' risk exposure and helping them make additional loans to small businesses.

- *Increasing the surety bond guarantee from $2 million to $5 million:*[28] This allows small businesses to better compete for federal construction and service contracts. Through SBA's Surety Bond Guarantee program, SBA guarantees bid, payment and performance bonds. Surety bonds protect the project owner against financial loss if contractors default or fail to perform. SBA partners with the surety industry to help small businesses that would otherwise be unable to obtain bonding in the traditional commercial marketplace. Under the partnership, SBA provides a guarantee to a participating surety company of between 70 and 90 percent of the bond amount.

- *Creating the American Recovery Capital (ARC) loan program:*[29] This provides no-interest, deferred repayment loans of up to $35,000 to help struggling, but viable, small businesses make debt payments. The ARC program carries a 100 percent guaranty from the SBA to the lender and requires no fees paid

[23] SBA's Economic Recovery Efforts and Impact: http://www.sba.gov/idc/groups/public/documents/sba_homepage/sba_rcvry_aara_imp_factsheet.pdf

[24] "Federal Financial Guarantees Under the Small Business Administration's 7(a) Program". http://www.cbo.gov/ftpdocs/87xx/doc8708/10-15-SBA.pdf

[25] SBA 504 Loan Program: http://www.sba.gov/financialassistance/prospectivelenders/cdc504/index.html

[26] SBA Recovery Act Programs Help Small Business in Tough Economic Times: http://www.youtube.com/watch?v=j95x571qtwk

[27] SBA Recovery Act Q/A for Small Business Owners: http://www.sba.gov/idc/groups/public/documents/sba_homepage/recovery_act_faqs.pdf

[28] SBA Surety Bond Guarantee: http://www.sba.gov/idc/groups/public/documents/wi_milwaukee/recoveryact_suretybonds.pdf

[29] SBA ARC Loan Program: http://www.sba.gov/recovery/arcloanprogram/index.html

to SBA. Loan proceeds are provided over a six-month period and repayment of the ARC loan principal is deferred for 1 year after the last disbursement of the proceeds. Repayment can extend up to five years.

Banking regulators have also responded to the need for small business credit. This took the form of the *Interagency Statement on Meeting the Credit Needs of Creditworthy Small Business Borrowers.* It instructs bank examiners not to discourage small business lending or criticize banks for working prudently with small businesses. Examiners are instructed not to reclassify a loan solely on basis of a decrease in the value of collateral, as long as the borrower shows a willingness and ability to repay their loans. Finally, examiners are not to classify loans solely because of difficulties in the borrower's industry or the region the borrower is located in. To the banking industry the guidance it offers is simple "To the maximum extent possible, loan decisions should be made based on the creditworthiness of the individual borrower, consistent with prudent management of credit concentrations."

Going forward, the Obama Administration has proposed using TARP funding for a separate Small Business Lending Fund. It would provide up to $30 billion in capital investments in banks with assets below $10 billion, for small business lending, with increased lending relative to 2009 base levels incentivized by dividend payouts as low as 1 percent.

New York State

In January 2010, Governor Paterson proposed the following programs to support small businesses in the 2010-11 New York State Executive Budget:

a. *$25 million Small Business Revolving Loan Fund:*[30] This program will provide loans to support the growth of small businesses. The fund would target minorities, women and other New Yorkers who have difficulty accessing regular credit markets. Funding would be seeded by a $25 million contribution from the New York Power Authority.

b. *$25 million in New Technology Seed Fund:*[31] This program will assist university-based entrepreneurs make the transition from pure research to the creation of marketable products. New York State is looking to fund start-up and early-stage small businesses that have demonstrated the most promising commercial potential in the fields of cutting-edge emerging technologies. Funding would be supported by the resources of the Job Development Corporation.

c. *Community Development Financial Institution (CDFI):* On March 24, 2010 in its Majority Resolution for a Fair and Responsible SFY10-11 Budget, the New York State Senate called upon Governor Paterson to direct $15 million for an initial capitalization of the New York State CDFI Fund.[32] Since CDFIs leverage Federal dollars with private dollars by an average of 20 to 1, the $15 million appropriation to the New York CDFI Fund will allow the state's CDFIs to leverage an additional $300 million in private sector investments.[33] Meanwhile in the New York State Assembly, there is a

[30] State of New York 2010-11 Executive Budget Briefing Book: http://publications.budget.state.ny.us/eBudget1011/fy1011littlebook/BriefingBook.pdf, p. 67.
[31] Ibid, p. 67.
[32] Credit Union Association of New York: http://readme.readmedia.com/New-York-Senate-Resolution-Includes-15M-for-State-CDFI-Fund/1222773
[33] Melanie Stern, Federation Senior Program Officer and Coordinator of the New York Coalition of CDFIs: http://readme.readmedia.com/New-York-Senate-Resolution-Includes-15M-for-State-CDFI-Fund/1222773

$1.5 million funding to expand CDFI lending to minority and women-owned business enterprises (MWBEs). [34]

d. *Excelsior Jobs Program:*[35] This program would provide job creation and investment incentives to firms in specific targeted industries such as biotechnology, pharmaceutical, high-tech, clean-technology, green-technology, financial services, and manufacturing. Businesses in these industries that create and maintain at least 50 net new jobs in New York for five years would be eligible for three tax credits, each of which is fully refundable:

- The Excelsior New Jobs tax credit of between $2,500 and $10,000 per new job to cover a portion of the associated payroll cost;
- The Excelsior Investment Tax Credit (ITC) valued at 2 percent return of total qualified investments; and
- The Excelsior Research and Development tax credit providing a 10 percent credit for new investments based on the Federal Research and Development credit.

New York City

The City's response to the credit crisis was two-fold: the NYC Business Solution Center and the Economic Development Corporation (EDC) Capital Access program.

a. *NYC Business Solution Centers:* The New York City Department of Small Business Services (SBS) assists small businesses through the NYC Business Solutions Centers (BSCs) in a variety of ways including business courses, legal review of contracts and leases, incentives, navigating government, recruiting and training employees, selling to government, and financial assistance.

As credit markets have tightened, more and more businesses are in need of capital. The BSCs assist businesses navigate the process of securing financing by helping customers understand the lending criteria, improve their credit scores if need be, and match the businesses with the right lenders. In 2008, the BSCs assisted 252 customers secure over $24.8 million in financing from large commercial banks, credit unions, and small micro-lenders.[36] In 2009 the BSCs assisted 404 businesses in securing over $22 million.[37] The median loan amount is $10,000 as opposed to $25,000 before.[38] A large share, more than two-thirds, were made with alternative lenders and credit unions, and were predominantly for operating businesses (as opposed to start-ups). SBS also saw more micro-lending of $1,000 to $2,000.[39] In 2010, the SBS Commissioner Robert Walsh is expecting to assist more than 500 customers secure financing.[40]

[34] New York State Assembly Fiscal 2010-2011 Budget Resolution.
[35] State of New York 2010-11 Executive Budget Briefing Book: http://publications.budget.state.ny.us/eBudget1011/fy1011littlebook/BriefingBook.pdf, p. 66
[36] Robert Walsh, Commissioner, testimony on SBS' Fiscal 2011 Preliminary Budget, March 18, 2010.
[37] NYC Business Solution Centers handout.
[38] Beth Fruchtman, Executive Director Program Management, and Daniel Koken, Program Associate, NYC Business Solution Centers, March 25, 2010 interview.
[39] Ibid.
[40] Robert Walsh, Commissioner, testimony on SBS' Fiscal 2011 Preliminary Budget, March 18, 2010.

b. *$5 million EDC Capital Access Program:*[41] This program provides up to a 40 percent guarantee on loans for qualified micro (under 20 employees) and small (21-100 employees) businesses trying to access loans. EDC has selected Citibank, Brooklyn Cooperative Federal Credit Union, Seedco, ACCION USA, and the Nonprofit Finance Fund as the five lenders in the program. Small businesses can access loans up to $250,000. Financing is available for retailers, manufacturers, wholesalers, non-profit organizations, contractors and distributors. Eligible uses include loan proceeds that are used for working capital, leasehold improvements and equipment purchases. To date, roughly $3 to $4 million has been allocated, leveraging $15 million in lending.[42] Funding is provided for operating capital, not for expansion. Most loans are micro-loans of roughly $5,000 to $10,000.[43]

c. *Municipal Deposits:* On March 25, 2010 the City Council unanimously passed Resolution 17, which calls upon the State legislature to enact legislation allowing local government entities statewide the option of depositing public funds in local credit unions or community savings institutions.[44] By allowing municipalities to deposit with credit unions, monies would stay and work in local communities. Expanded depository choice would also add funds to a lending pool that has been somewhat scarce at big banks, and increase revenues for cities and towns-in turn, creating savings for New York taxpayers. It would also enable credit unions to offer lower loan rates and create more affordable loan products for their communities.

B. Private/Voluntary sector responses

Seedco Programs

In November 2009 Seedco Financial announced a five-year $20 million grant partnership with Goldman Sachs to help 10,000 small businesses through Seedco Financial's "NYC Small Business Support Initiative."[45] The funding will provide for capacity building, technical assistance, and access to loan capital to underserved, low-to-moderate income, small businesses and also minority and women-owned business enterprises. The loan capital will develop place-based, micro-targeting strategies in commercial and retail corridors that do not typically qualify as areas of economic distress.[46] The program will create a "Business Expansion Loans" to provide critical funding for businesses with a three-year operating history, a minimum of $300,000 in annual revenues, at least five employees and an engaged management team.[47] This program will focus on providing capital and resources for small businesses to expand sales, and operating capacity in growth sectors such as clean technology and weatherization.

[41] NYC EDC Capital Access Loan Guaranty Program: http://www.nycedc.com/FinancingIncentives/Financing/NYCCapitalAccessLoanGuarantyProgram/Pages/NYCCapitalAccess.aspx
[42] Andrew Barnes, Assistant Vice President, EDC interview March 26, 2010.
[43] Ibid.
[44] Credit Union Association of New York: http://readme.readmedia.com/NY-City-Council-Passes-Resolution-in-Support-of-Municipal-Depository-Choice/1217549
[45] Seedco's $20 million partnership with Goldman Sachs: http://www.seedco.org/press/pressreleases.php?id=118
[46] Ibid.
[47] Ibid.

Credit for Success Program

The New York Business Development Corporation (NYBDC) and the New York Bankers Association (NYBA) have initiated a program called "Credit for Success" in response to the credit crisis.[48] The program brings together member banks in regional lending consortiums to provide an additional lending facility, backstopped with loan guarantees, to businesses whose loan applications were declined by their banks of account. This "Second Look" will be combined with business counseling to identify creditworthy small businesses that are otherwise shut out of access to credit markets. The risk-sharing inherent in a consortium, along with NYBDC participation, will help extend lending to eligible businesses that a single bank might not extend credit to.

Eligible uses for Credit for Success loans include refinancing, working capital, and equipment purchases. Loan amounts range from $25,000 to a maximum of $150,000. Applicants must meet U.S. Small Business Administration (SBA) eligibility requirements and agree to seek business counseling from the regional Small Business Development Center. All loans are guaranteed by the SBA for at least 85 percent of the principal amount of the loan.

Regional consortiums have been created in several areas of New York State, including Albany, Binghamton, Buffalo, the Hudson Valley, the North Country, Rochester, and Syracuse. As of now, no consortium has been created for New York City.

Conclusion

The financial crisis has made credit harder to get for small businesses. Even strong businesses with sound business plans and steady revenue might not qualify for a loan at a time when banks see increasing delinquencies on the small business loans they are carrying and capital requirements are rising. Programs at all levels of government have been implemented to mitigate these problems and to create additional capacity for small business lending in an environment that is trying for both borrowers and lenders.

Small businesses will provide many of the jobs that will bring the unemployment rate down. They are also a source of innovation and can be a source of economic diversification. It is critical that creditworthy borrowers have access to credit now. Assuring fair loan origination will create an environment that fosters the growth of new small businesses as the economy recovers.

There are existing resources to assist New York City small businesses with access to credit. Locally, these include the Department of Small Business Services' New York City Business Solution Centers, the New York City Economic Development Corporation's Capital Access Program, Seedco Financial's "Small Business Support Initiative" with Goldman Sachs, and the "Credit for Success Program" by the New York Business Development Corporation and the New York Bankers Association. With so many small businesses struggling, uptake and efficient use of these programs is increasingly important. It requires developing the tools for financial institutions and government to communicate regularly and effectively with each other and with small businesses.

[48] New York Business Development Corporation's Credit for Success: http://www.nybdc.com/documents/RegionalLendingConsortiums-WebContentwithLogo.pdf