



MEMORANDUM

Prepared for: House Committee on Economic
Development
Date: February 19, 2020
By: Melissa Leoni, Analyst
Re: Loan Loss Comparisons

LPRO: LEGISLATIVE POLICY AND RESEARCH OFFICE

Chair Lively has asked for a comparison between the existing Capital Access Program at Business Oregon, the Community Lender Loan Loss Program described in House Bill 4033, and the lender loan loss account awards program that will be included in the -2 amendments to House Bill 4033.

SUMMARY

A loan loss provision is a set-aside for uncollected loans that can be the result of a number of factors associated with potential loan losses, including bad loans due to customer defaults, unrecoverable collateral, or losses attributed to unsecured lending.¹ Table 1 on the following pages contains a comparison of the program purposes, processes, eligibility criteria, loan requirements, loan loss contributions, outcomes, evaluation, and other conditions for each loan loss program or approach.

¹ Business Oregon, *Loan Loss Reserve Provision and Capital Access Program Overview*, <https://olis.oregonlegislature.gov/liz/2020R1/Downloads/CommitteeMeetingDocument/212869>.

Table 1: Loan Loss Reserve Programs and Lender Loan Loss Account Comparison

Program	Capital Access Program (CAP)	HB 4033 Community Lender Loan Loss Program	-2 Amendment Lender Loan Loss Accounts
General Description	The CAP, created in 1991, provides a form of loan portfolio loss reserve to enable financial institutions to make higher risk business loans while complying with federal and state banking regulations. ²	The purpose is to establish a community lender loan loss account program under which the State of Oregon will provide public funding to assist Oregon lenders to overcome obstacles and constraints in meeting the full range of economically sound financing needs of Oregon businesses.	The purpose is to make awards to qualified lending institutions to fund lender loan loss accounts to increase lending to business owners and entrepreneurs who currently lack access to capital to start or grow their businesses, including businesses owned by women, minorities, veterans, low income persons and persons operating businesses in rural areas of the state.
Overall Process	<p>Business Oregon has adopted program rules (OAR 123-018). A lender applies to enroll a loan in the program (application form). The department reviews the application to ensure the project and credit structure is eligible. If additional documentation is needed, the department the lender for more information. Once a loan is deemed eligible, the department determines if it is eligible for a single or double match based on program criteria and supporting documentation. Requests for payment are submitted to the department accounting team and the payment is mailed the following business day.</p> <p>The lender submits claims for reimbursement of qualified loan losses to the department and demonstrates losses are eligible (claim form). The department approves or denies the reimbursement claim.</p>	<p>Business Oregon adopts program rules, including for providing the double match for certain borrowers and for submitting claims for loss reimbursement. The department enters into contracts with eligible lenders to participate in the program. Loan loss accounts are established and maintained by the department for the benefit of participating lenders. All the moneys in the account are the property of the State of Oregon.</p> <p>A lender applies to enroll a loan in the program on a loan-by-loan basis within seven days of making a qualified loan. Department reviews the loan application and lender credit memo to ensure the project and credit structure are eligible. If additional documentation is needed, the department asks the lender. Once a loan is deemed eligible, the department determines if it is eligible for a single or double match based on program criteria and supporting documentation.</p> <p>The lender deposits borrower loan loss fees into the loan loss account. The request for state payment is submitted to the department and the match payment is made to the account.</p> <p>The lender submits claims for reimbursement of qualified loan losses to the department and demonstrates that losses are eligible. The department approves or denies the reimbursement claim.</p>	<p>Business Oregon makes awards through a competitive RFP process to eligible lenders to fund a lender loan loss account. A committee of stakeholders with relevant experience from the financial industry, economic development professionals, and federally recognized tribes assist the department in reviewing proposals and making recommendations for funding.</p> <p>Business Oregon enters into written agreements with each lender awarded funds. The agreement requires setting up the loan loss account, tracking loans that will be reimbursable from the account, depositing borrower loan loss fees in the account, liquidation of borrower assets before the reimbursement of losses from the account, and annual reports.</p> <p>Lenders report annually to Business Oregon who then reports to the Legislative Assembly. After complying with certain requirements, lenders may be released from the agreements and use the account balance for any purpose.</p>

² Business Oregon, *Oregon Capital Access Program*, <http://www.oregon4biz.com/How-We-Can-Help/Finance-Programs/CAP/>.

Program	Capital Access Program (CAP)	HB 4033 Community Lender Loan Loss Program	-2 Amendment Lender Loan Loss Accounts
Lender Eligibility	Only regulated financial institutions (banks and credit unions) are eligible. Currently the following are CAP enrolled lenders: Beneficial State Bank, Bank of the Pacific, Columbia Bank, First Interstate Bank, Lewis & Clark Bank, and Old West Federal Credit Union. ³	Lenders must be a government agency or a nonprofit corporation as defined in ORS 307.130; be mission-driven; have at least five years of physical presence and operations in Oregon; and provide financial and technical assistance to small businesses, microenterprises and start-up businesses.	Lenders eligible for an award must be certified as a community development financial institution, a nonprofit corporation, or affiliated with an economic development district or local government; have a physical presence in Oregon; and at least five years of lending experience. Financial institutions defined in ORS 706.008 are not eligible to apply. Proposals for an award must include information on past lending performance, projected loan production with the award, how the award increases the lender's capacity to make loans to underserved businesses, and the extent the lender provides technical assistance to borrowers.
Loan Eligibility	All types of loans and lines of credit are eligible. The program is designed for non-profit and for-profit businesses seeking funds for most business purposes. Eligible loans may not be used to purchase or improve residential housing, purchase or improve real property not used for business operations, or refinance an existing balance of a non-enrolled loan.	Loans can be made to qualified businesses (borrower) legally doing business in Oregon and with 20 or fewer employees. The maximum amount for eligible loans is \$300,000. Defines eligible loans as loan or portion of a loan made by a lender to a qualified business for any business activity that has its primary economic effect in Oregon. Prohibits loans for the purchase or improvement of residential housing; for the purchase or improvement of real property not used for business operations; for working capital for terms exceeding five years; for fixed asset terms exceeding the useful life; with a variable interest rate or rate over prime plus five percent; or for refinancing certain loans.	'Reimbursable loan' means a loan or portion of a loan made by a lender to a qualified business the losses from which are reimbursable from moneys in the lender's loan loss account. The loans not eligible to be a reimbursable loan are similar to CAP and the base bill program.
Interest Rates and terms	Rates and terms are established by lender.	An eligible loan must have fixed interest rates with an interest rate cap of prime plus five percent.	Eligible reimbursable loans must have fixed interest rates with a cap of prime plus six percent.
Loan Loss Contributions	The lender and borrower contribute three to seven percent to the lender's loan loss reserve account, which is matched by Business Oregon. The state's maximum contribution is \$35,000 per borrower.	The borrower contributes three percent to the lender's loan loss account and the fee may be paid out of the loan proceeds. The state's maximum contribution for any single loan is \$7,500 or \$15,000 for a double match.	The agreement between the department and lender requires any fees directly related to the designation of the loan as a reimbursable loan to be deposited in the loan loss account. Lenders set the fee rate.

³ Business Oregon, *Oregon CAP Enrolled Lenders*, <http://www.oregon4biz.com/How-We-Can-Help/Finance-Programs/CAP/Lenders/>, last visited February 19, 2020.

Program	Capital Access Program (CAP)	HB 4033 Community Lender Loan Loss Program	-2 Amendment Lender Loan Loss Accounts
State Processing	The department reviews loan applications and makes eligibility determinations. The total processing time for complete CAP applications is estimated to be between 24 and 48 hours. ⁴	The department contracts with eligible lenders and conducts loan application review and eligibility determination. The processing time is assumed to be similar to CAP.	The department is responsible for the RFP review and award process, development of lender agreements, tracking submission of lender annual reports, and submission of an annual report to the Legislative Assembly.
Outcomes	<p>CAP outcomes for the 2015-2017 biennium:⁵</p> <ul style="list-style-type: none"> • Enrolled 44 loans matching \$92,146 in borrower and lender fees; • Average enrolled loan of approximately \$60,000; • Leveraged \$2,628,695 in private funding; • Projected to create and retain 186 jobs; • 60 percent of loans were made outside of the Portland metropolitan market; and, • Average of six employees per borrower. 	The lender provides annual reports to the department on the lender's loan activity, financial statements and tax filings, and other required information.	<p>Each lender is required to submit an annual report to Business Oregon by July 31 for the previous fiscal year on:</p> <ol style="list-style-type: none"> 1. The number of and principal amounts of reimbursable loans; 2. The interest rate and term of loans; 3. The amount loaned that would not otherwise have been loaned without the account; 4. The ratio of total principal loaned to the lender's award; 5. The amount of money withdrawn from the account for losses; 6. Location, employment, and demographic information on borrowers; and 7. Outreach conducted. <p>Business Oregon is required to report annually by September 15 to the Legislative Assembly on the awards made, aggregated lender and borrower data, aggregated loan performance, average interest rates and terms, and locations of borrower businesses.</p>
Other Criteria or Conditions		<p>The program limits cumulative balances in the loan loss account and requires payment of certain balances with the annual report. The loan loss account is terminated if it is dormant for more than 12 months. The sale, transfer, or assignment of loan loss accounts or loan loss reserve portfolios is prohibited, and repayment of the balance is required if that occurs.</p> <p>The bill creates a Community Lender Loan Loss Account Fund for deposit of the state appropriation to be used as the match for qualified loans enrolled in the program.</p>	<p>For the lender awards, no more than 10 percent of the funds may be awarded to a single lender, and no more than 40 percent may be awarded for use by businesses in the three counties of the Portland metropolitan area.</p> <p>The amendment requires repayment to the General Fund of the balance of awarded funds if the lender has not made reimbursable loans for 24 consecutive months; becomes insolvent; fails to perform materially; makes material misrepresentations; or sells, transfers, or assigns the account or loan loss portfolio.</p>

⁴ Business Oregon, *Loan Loss Reserve Provision and Capital Access Program Overview*, <https://olis.oregonlegislature.gov/liz/2020R1/Downloads/CommitteeMeetingDocument/212869>.

⁵ Business Oregon, <https://olis.oregonlegislature.gov/liz/2019R1/Downloads/CommitteeMeetingDocument/154372>

Program	Capital Access Program (CAP)	HB 4033 Community Lender Loan Loss Program	-2 Amendment Lender Loan Loss Accounts
Program Evaluation	None required.	None required.	The amendment requires an interim committee on economic development to evaluate the effectiveness of the lender loan loss account program by September 15, 2022 and develop recommendations for the 2023 legislative session. The committee is required to consult with the lenders who receive the awards and consider the annual reports submitted by Business Oregon.