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# Make No Little Plans: How a Midwest Bank Uses a Capital Access Program to Help Small Businesses

by Thomas Doherty, *Group Senior Vice President, Midwest Business Banking Division, LaSalle Bank, N.A.*

*There are over 40 Small Business Development Centers in Illinois which provide technical assistance to potential Capital Access Program borrowers.*

When it comes to supporting the growth of small businesses, Chicago-based LaSalle Bank heeds the advice of the legendary Chicago architect Daniel Burnham. "Make no little plans," he famously said, and we think that's a good way to pursue our strong and well-established commitment to small business development. It's also good advice for our small business clients. We harness Burnham's maxim to a related objective: Keep things as simple as possible — including all aspects of financial planning and financing.

One way we are able to do that is by participating in Illinois' Capital Access Program (CAP), which is designed to provide access to capital for businesses that cannot qualify for conventional bank financing. We like the CAP because it's consistent with our strategy of streamlining our banking and lending processes and helping our small business clients remain unencumbered by lengthy, complex loan applications. Think of the CAP as an equalizer: by greatly simplifying the entire loan process, it can make lending to small borrowers as cost-effective as lending to larger businesses.

### *Pooling risks*

Structurally CAPs differ from conventional loan guarantee programs in which a percentage of a loan is guaranteed on a loan-by-loan basis. CAPs, in contrast, rely on risk-pooling. The insurance provided by a loan reserve enables participating banks to make loans that would not meet their conventional underwriting standards.

The process is straightforward. The bank develops a portfolio of loans to be insured by the reserve. The bank then merely notifies the state of its enrolled loans, and the state matches the borrowers' contributions to the loan reserve. The bank uses its standard closing documents and a CAP representation form, which acknowledges the borrower's acceptance and fee charged for the program. This is the only governmental document requiring the borrower's signature.

The Illinois Department of Commerce and Economic Opportunity (DCEO) has streamlined the process to such a degree that our borrowers experience hassle-free loan closings. That is very important to small business owners who must be able to stay focused on running their businesses rather than getting bogged down in paperwork.

Each time a loan is enrolled under the program, a one-time premium is paid by the borrower, ranging from 3 percent to 7 percent of the total loan amount. The bank determines the reserve fee, and DCEO matches that amount dollar for dollar. The more loans the bank makes, the more it builds the reserve fund, thereby enabling it to make more relatively high-risk loans. The maximum loan size under the Illinois program is $100,000 and term loans or lines of credit are eligible for consideration.

In the five years since LaSalle began participating in the program, we have enrolled $11.4 million in loans. Our average loan size is approximately $38,000. LaSalle's CAP loans have helped create more than 900 new jobs and have kept more than 1,000 jobs intact in Illinois.

CAP borrowers typically are emerging businesses lacking the kind of track record they would normally need to establish eligibility for a conventional loan. Often they need working capital, but lack the necessary collateral, or the principals have insufficient personal assets. They are unlikely to be able to attract venture capital or private equity. But these businesses often are the backbone of their communities. Supporting them is the right thing to do, and a CAP loan is often the right way to meet their needs.

Typically CAP clients have less than $1 million in revenues and need less than $100,000, in credit. In most cases, we can charge a 3 percent to 7 percent reserve fee, below the 7 percent maximum under the state's guidelines. Borrowers can finance the fee from loan proceeds. Most loans are enrolled with the state for up to four years, subject to the bank's annual review, and term loans are enrolled for the full amortization of the loan. The bank's interest rate is marketplace-competitive.

***Small business banking that works***

Statewide, the Illinois Capital Access Program originated $101 million in loans from February 1997 through August 2003, 72 percent of them to businesses with annual sales below $1 million; 43.5 percent went to businesses owned by women, minorities, or persons with disabilities. The state estimates that those loans created 6,039 jobs.

We view this as a vitally important program. We are investing in the future — of our bank as well as our state — by providing the capital that small businesses need to help them flourish over the long term. In line with LaSalle's commitment, we participate in various community outreach seminars designed to disseminate information on business products and services, and partner with local business development groups working to sustain emerging businesses. We also publish an extensive small business resource guide that profiles all the governmental programs available. And as long as the Capital Access Program remains viable, we plan to participate.

*For more information, please contact Thomas Doherty at (773) 244-7473, Thomas.Doherty@abnamro.com, www.lasallebank.com.*

## CAPs: A Simple and Effective Way for Banks to Aid Small Businesses

Capital Access Programs (CAPs) are pooled loan programs that are administered by either state or local agencies (20 states and two municipalities operated these programs in 2001 according to the Department of Treasury). CAPs have several attractive features:

- They enable banks to make moderately risky small business loans with a minimum of administrative paperwork and associated costs.
- Banks use their own underwriting standards to make loans. No government approval is required.
- Because overhead costs are very low, CAPs offer a cost-effective way to make the kinds of relatively small loans (typically under $100,000) that many small business start-ups and expansions desperately need.
- Although CAP loans are not guaranteed, loan reserves can insure against loan losses.
- States can use their CAPs to target loans to areas or groups especially in need of greater access to capital.

When a small-business borrower does not meet conventional lending criteria, a bank may offer the borrower a CAP loan carrying an "insurance premium," generally 3 percent to 7 percent of the loan amount. The bank may also contribute to this premium. Typically, the state will match the combined contributions, and some states match at higher rates for loans going to lower-income areas or businesses owned by women and minorities. The premiums collected by the bank go into a CAP reserve account that the bank holds. If a CAP loan fails, the bank can draw down the reserve to cover the loss, but it is responsible for losses exceeding the reserve. This approach gives the bank leeway to make reasonably — but not unduly — risky loans.

Administrative simplicity is a CAP hallmark. Unlike loan guarantee programs, there is no requirement for the government to review of each loan. Instead, the bank merely transmits a one-page enrollment form to the state, which transfers its matching contribution to the bank.

Michigan pioneered the first Capital Access Program in 1986. A 1999 study by Michigan State University found that the state CAP had generated more than 5,000 business loans valued at $286.8 million. About 86 percent of the loans were to businesses with annual sales under $1 million. More than 20 percent of the loan recipients reported that they could not have obtained financing without the CAP and would have gone out of business without the CAP loan.

A nationwide study by the Department of the Treasury in 2001 (see *Capital Access Programs: A Summary of Nationwide Performance*, www.treas.gov/press/releases/docs/cap01.pdf) the latest such analysis available, found that as of June 2000 cumulative CAP lending nationwide topped $1.5 billion, with nearly 400 banks originating CAP loans. Concluding that CAPs "encourage small-business lending in a cost-efficient and simple way," the study also noted that CAP loans were reaching "some groups of borrowers not as well-served by other credit enhancement programs," including minority-owned businesses and businesses located in targeted low- and moderate-income areas.

A Web listing of states with CAP programs is available at:
http://smallbusinessschool.org/webapp/sbs/basics/money/capitalaccess.jsp