CDFA Michigan Financing Roundtable

# 2010 Economic Development Finance Conference

March 30, 2010 Detroit, Michigan

The CDFA Michigan Financing Roundtable is dedicated to developing a sustainable economic development finance industry for the state of Michigan.

A collection of CDFA members and finance leaders from across the state, the Roundtable brings together the development finance industry through education, news and research.

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# About CDFA

- National non-profit association representing the development finance industry.
- Provide education, advocacy, research, networking and leadership.
- Training Institute – Bond Finance (2), Tax Increment Finance (2), Tax Credit, Revolving Loan Fund Finance, Innovation Finance and Fundamentals of ED Finance Course.

# About CDFA

- Research – Produce annual State-By-State studies for Bond Volume Cap and Tax Increment Finance Statute changes.
- Resources – Over 5000 resources online through our Bond, TIF, Tax Credit and RLF libraries.
- Advocacy – Active partner with Congress and Administration and had 3 items in the 2009 stimulus bill.

# Today’s Schedule

- Housekeeping Reminders
- Agenda
- Presentations Online
- Resources Online

# Unlocking the Development Finance Toolbox

# What is Development Finance?

- Development finance is the efforts of local communities to support, encourage and catalyze economic growth through public/private investment in physical development, redevelopment, business and industry.

- It is the act of contributing to a project/deal that causes that project/deal to materialize in a manner that benefits the long term health of the community.

# What is Development Finance?

- Development finance requires programs and solutions to challenges that the local environment creates.
- Economic developers are the bridge between government and business and often direct the vision of a sound financing toolbox.
- Regional advantages can enhance development finance efforts through partnership, cooperation and mutually advantageous programming.

# What Does DF Include?

- Debt, equity, credits, liabilities, remediation, guarantees, collateral, credit enhancement, venture/seed capital, early stage, workforce, technical assistance, planning, short-term, long-term, incentives, gap, etc.
- Proactive approaches that leverage public resources to solve the needs of business, industry, developers and investors.

# What DF *Does Not* Include

- Free handouts and unabashed subsidies
- Creating a competitive environment
- Duplicative assistance
- Poor due diligence and transparency
- Poor oversight and performance measures
- Irrational responses to immediate challenges

# Why is DF Important?

- Businesses need working capital and the ability to invest in themselves.
- Developers need assistance to achieve an acceptable ROI.
- Communities need infrastructure and amenities.
- Citizens need opportunities for advancement – jobs, small business, education, etc..
- Regions need economic prosperity.

# Trends in DF Tool Use

- 50% of finance agencies issue bonds
- 41% act as conduit bond issuers
- 50% provide direct loans
- 27% provide loan guarantees (collateral support)
- 39% provide grants
- 62% provide technical assistance

# Despite these Trends

- 50% of all finance agencies allocate less than 20% of their actual budget to directly financing development. Why?

# 2006 Tool Use Trends

- **Industrial Development Bonds (IDBs):**
  Only 27% of agencies frequently use with 50% rarely or never using.

- **Tax Increment Finance:**
  Nearly 40% of finance agencies do not use TIF (49 states have TIF capabilities).

- **Tax Credits:**
  Less than 5% of finance agencies frequently employ the use of state & federal tax credit programs.

# 2006 Tool Use Trends – Abatements

- Nearly 50% of agencies are actively using tax abatements (this is a declining trend).
- Clawbacks and greater scrutiny is finally emerging.
- The competitive “arms race” atmosphere is slowing down (but far from gone).

# 2006 Tool Use Trends – RLFs, etc.

- Over 43% of agencies use frequently
- RLFs represent the single most used finance concept nationally yet these tend to be largely overlooked and underutilized (and under appreciated).
- 26% of agencies have an RLF dedicated strictly to small business loans.

# 2006 Tool Use Trends – Federal

- CDBG – 40% frequently use
- EDA – 18% frequently use
- Reliance on federal funding remains strong yet this source is the most volatile and less reliable from year to year.
- A note on grants – over 25% of agencies are actively providing grants to finance development.

# So What is Happening Here?

- Why are agencies ignoring tried and true tax-exempt bond financing tools for addressing manufacturing & non-profit development?
- Why are economic developers ignoring targeting financing tools such as TIF for addressing redevelopment, business district and revitalization?

# So What is Happening Here?

- Why are tax credits programs underutilized? Tax credits abound – NMTC, brownfields, historic, LIHTC, hundreds of replicable state program.
- Nearly 30 states have state sponsored venture funds. Why is there little connection?
- Why the reliance on federal funding?

# A Few Answers

- Complexity of financing programs
- Nature of locally controlled, political economic development efforts
- Lack of focus on financing strengths within community
- Little dedication to education and capacity building

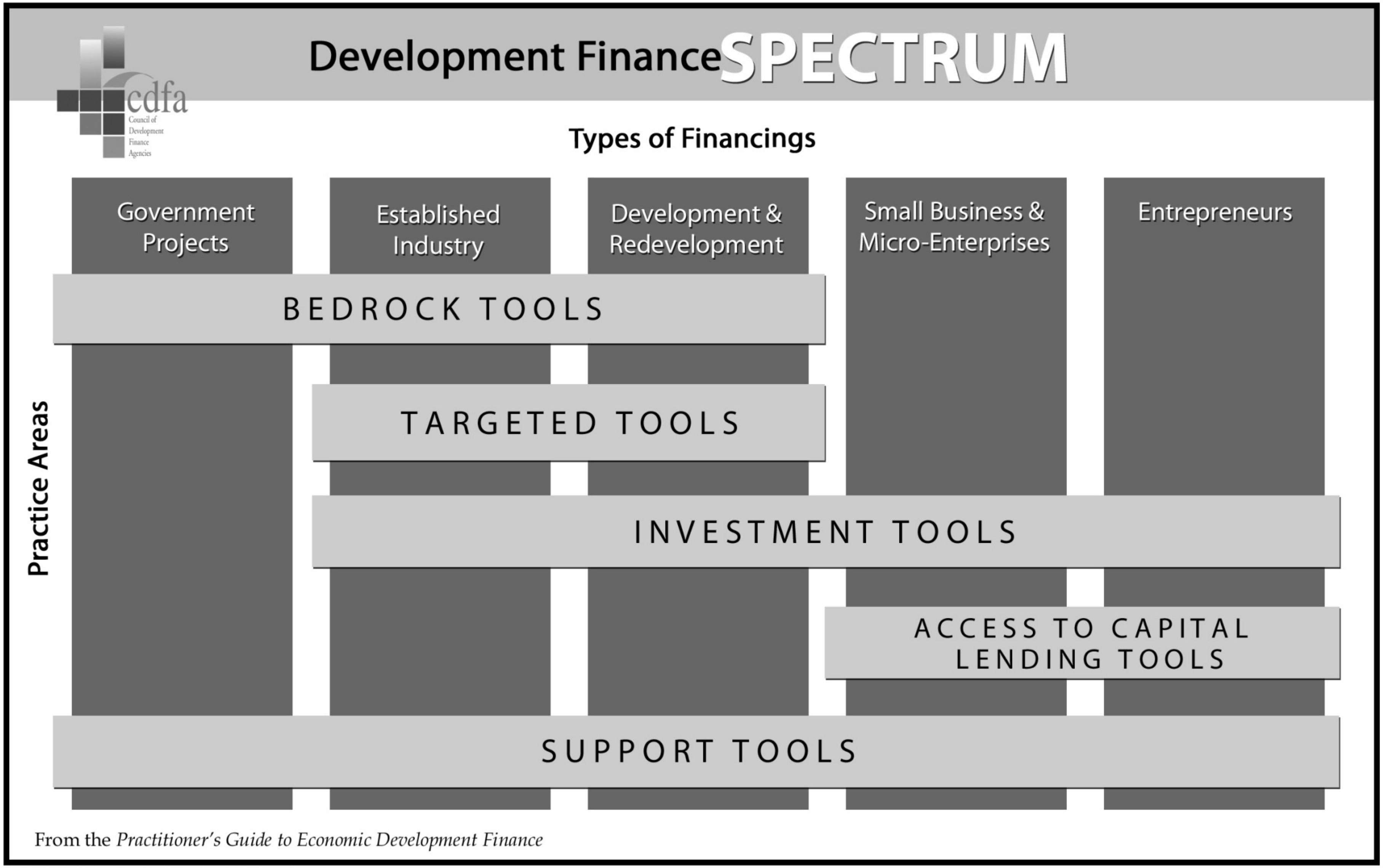
# Public or Public/Private

- Public – 81% of public agencies allocated less than 20% of their budget directly towards financing development.
- Public/Private – 33% of public/private agencies allocate over 50% of their budget directly towards financing development.
- Consider your structure closely.

# Development Finance Spectrum

- Every project presents a different financing challenge or opportunity.
- Large scale industrial development requires a different financing approach when compared to small business development.
- Some financing options (such as RLFs) may address a wide range of financing needs.
- Understanding the development finance spectrum is critical to employing the toolbox approach.

# Development Finance Spectrum



# In the End…

- All economic development comes down to access to capital and other financial resources for completing a given project or deal.
- Nearly all projects and deals hinge on the ability to leverage inexpensive sources of financing.
- As they say…cash is king, money makes the world go around and show me the money!

# Introducing the Toolbox Approach

- The toolbox approach is a full scale effort to building local and regional financing capacity to serve and impact a variety of business and industry financing needs.

- This is an investment in programs and resources that harness the full development finance spectrum of a community's financial resources and is a dedication to public/private partnerships.

# Why the Toolbox Approach?

- Partnership development is a theme of the toolbox approach. More parties can be involved – banks, thrifts, educational providers, investors, angels, developers, planning authorities, bond counsel, trustees, special authorities, CDFIs, CDCs, EDOs, MPOs, RPOs, etc.

- Diversity is very important in development finance efforts.

# The Toolbox and Financing Spectrum

5 Practice Areas

**Practice Area 1: Bedrock Tools**

- Bonds and the Basics of Public Finance

**Practice Area 2: Targeted Tools**

- Tax Increment Finance, Special Assessment Districts, Government Districts and Project Specific District Financing

# The Toolbox and Financing Spectrum

**Practice Area 3: Investment Tools**

- Tax Credits, Seed & Venture Capital and Angel Funds

**Practice Area 4: Access to Capital Lending Tools**

- Revolving Loan Funds, Mezzanine Funds, Loan Guarantees and Microenterprise Finance

**Practice Area 5: Support Tools**

- Federal Funding and Abatements

# The Toolbox in Action

Brian Holdwick
Executive Vice President
Detroit Economic Growth Corporation

Questions?

# *Practice Area 1:*

# *Bedrock Tools*

# Bedrock Tools

- Bond use dates back over 90 years with the tax reform act of 1986 shaping today's use
- Communities pledge tax revenues to back "loans" basically through Government (GOs) & Private Activity Bonds (PABs)
- GOs are tax-exempt, used for public projects
- PABs can be tax-exempt, utilized for economic development

# Variety of PABs

- Exempt Facility Bonds – Can be used for airports, docks, wharves, mass-community facilities, etc.
- Qualified Redevelopment Bonds – Infrastructure projects that do not meet the requirements of GOs may qualify for tax-exemption if they meet several tests of "qualified redevelopment bonds; " e.g., proceeds used for redevelopment purposes in designated blighted areas, etc.

# Variety of PABs

- Qualified 501(c)(3) Bonds – Bonds used to finance projects owned and used by 501(c)(3) organizations. Two types - hospital bonds and nonhospital bonds
- Qualified Exempt Small Issues – IDBs for qualified manufacturing projects including purchase, construction, extension and improvement of warehouses, distribution facilities, industrial plants, buildings, fixtures and machinery.

# Variety of PABs

- Aggie Bonds - Support beginning farmers and ranchers with eligible purchases of farmland, equipment, buildings and livestock.

- Other Revenue Bonds – Allow revenue-generating entities to finance a project and then repay debt generated revenue. Toll roads and bridges, airports, seaports and other transportation hubs, power plants and electrical generation facilities, water and wastewater (sewer).

# Variety of PABs

- Enterprise Zone Bonds – Issued for projects in designated EZ communities. Bond proceeds may be used to finance projects for commercial facilities as well as manufacturing.
- Mini Bonds – Lower fees and streamlined program
- Others include CREBs, Green & GO Zone bonds
- Recovery Zone Bonds and Build America Bonds

# Why Communities Use PABs?

- Opportunity to invest in projects and businesses and the ability to influence ROI in development projects
- Easy to promote and monitor with performance measures
- Low cost and secure source of support for industry
- Can issue on conduit basis without backing (IDBs)

# Why Industry Uses PABs?

- Lower interest rates (conventional loans vs. tax-exempt)
- Tax-exempt status to buyers of bonds – attractive
- Lower cost to borrower
- Cheaper money (but not free)

# Notes on PABs

- Market forces at play – when traditional interest rates are low IDBs tail off, when traditional interest rates go up, IDBs go up
- Need good bond counsel on transactions – don't risk an issuance going taxable if it is not a qualified PAB
- Many rules and regulations – learn the programs before making any determinations

# Bedrock Tool Resources

- CDFA Resources:

  - Bond Finance Resource Library
  - National Volume Cap Resource Center

  - Intro Bond Finance Course
  - Bond Finance Reference Guide

  - Advanced Bond Finance Course – May 10-11, 2010
  - Advanced Bond Finance Reference Guide

# Practice Area 3:

# Investment Tools

# Investment Tools

- These tools provide incentives for individuals and companies to make investments in the community.
- Federal and state governments have created programs with both targeted and broad based functions.
- Two general types of programs:

1. Tax credits
2. Innovation finance

# About Tax Credits

- Response to dwindling federal resources for financing development over the past 15 years.
- Hundreds of programs have emerged based on the need for niche financing.
- Can help capitalize new business ventures or solidify financing for real estate projects.
- Increase a projects return on investment (ROI).
- Fill many gaps in the marketplace (brownfields, new markets, historic, housing, etc.).

# Basics of Tax Credits

- Investors receive a state/federal credit on their tax liability for qualified cash investments in projects or deals.

- Investors must demonstrate, with written proof, that the resource commitment has been made and in turn the distributor of the tax credit is only authorized to issue credit based on actual outlays of these resources.

# Basics of Tax Credits

- Investor then takes the credit on govt. tax liability. Can be personal, business, corporate or other liability depending on state and circumstances.
- In some cases, the credit is transferable to others through sale creating a secondary financial market, thus encouraging more investment.

# Main Federal Programs

- Historic Rehab Tax Credit
- New Markets Tax Credit
- Federal Brownfield Expensing Tax Incentive

Lesser known:

- Renewal Communities/Empowerment Zones
- Wind and Renewable Energy Credits
- Business Energy Tax Credits

cdfa Council of Development Finance Agencies

# Investment Tool Resources

- CDFA Resources:

  - Tax Credit Finance Resource Library

  - Intro Tax Credit Finance Course – November 11-12, 2010
  - Tax Credit Finance Reference Guide (November 2010)

  - Innovation Finance Course – Coming in 2010
  - Innovation Finance Reference Guide (Late 2010)

# Practice Area 4:

# Access to Capital Lending Tools

# Access to Capital Lending Tools

- Small businesses make up 99.7% of all firms, employ half of all private sector employees and account for 45% of the total U.S. payroll.
- Small businesses have also generated 60-80% of all new jobs annually over the past decade.
- Economic developers, however, have traditionally neglected small business development in pursuit of larger companies.

# Access to Capital Lending Tools

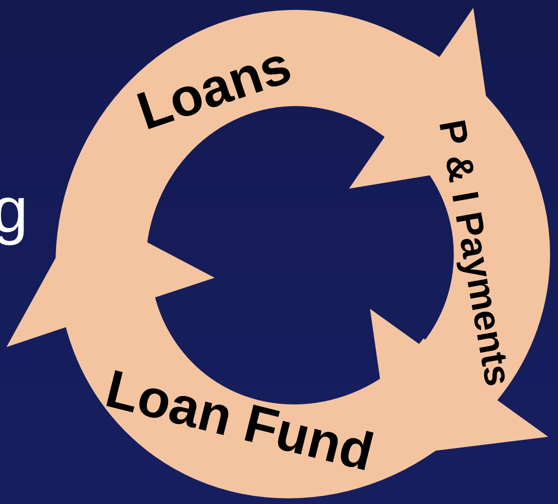
- Small businesses need access to affordable, reliable capital to get started, for their day to day operations and for new investment.
- They need “working capital”, to get through on a day to day basis.
- Communities that offer access to capital options are building relationships with their small business community as a partner and investor.

# Access to Capital Lending Tools

- Access tools cover a wide variety of programs that are tailored to address specific industry needs, for businesses in different stages of development, largely at the local level. They can include:
  - Revolving Loan Funds
  - Mezzanine Funds
  - Loan Guarantees
  - Linked Deposit Programs
  - Microenterprise Finance

# Revolving Loan Funds

- Gap financing measure primarily used for development and expansion of small businesses which are unable to obtain financing through traditional sources.
- Uses both public and private sector funds for capitalization (federal resources available).




- Self-replenishing pool of money, utilizing interest and principal payments on old loans to issue new ones.
- RLFs don't compete with convention funding sources, they compliment them.

# Access Tools – Mezzanine Funds

- Gap financing measure for growth-oriented small businesses that may not entirely qualify for loans or investments through traditional lending.

- Mid-level financing – Less risky than equity or venture capital but more risky than senior bank debt.

- Business usually has to cede some management or institutional control or give an ownership position to lender.

# Loan Guarantees

- Allows private sector to make loans and investments without carrying higher levels of risk.
- These programs shift risk from private sector to a third party – typically a governmental entity – by “guaranteeing” a portion of a loan or revenue source.
- Federal government operates several programs while states and cities are also now providing guarantees.
- Communities with strong balance sheet should consider building a program for projects that may need additional collateral support.

# Microenterprise Finance

- Microenterprises are the smallest of the small businesses. Typically defined as business with:

  - 5 or fewer employees
  - Capital needs of less than $35,000
  - Average loans of $7,000

- 24 million microenterprises in the U.S.

- Perceived by lenders as having a very high level of risk.

# Microenterprise Finance Programs

- SBA Microloan Program – Provides very small loans to start-up, newly established, or growing small businesses. SBA makes funds available to nonprofit community based lenders (intermediaries) which, in turn, make loans to eligible borrowers in amounts up to $35,000. The average loan size is about $13,000. Applications are submitted to the local intermediary and all credit decisions are made on the local level.

- NSF SBIR/STTR – Provide competitive grants for small business development for high-tech and innovation industry business development.

# Federal Small Business Lending

- SBA 504 Loan Program
- Operated through Certified Development Companies which can work in a state, region or nationally. Approximately 300 CDCs nationwide.
- Oklahoma
  - Metro Area Development Corp.
  - Rural Enterprises of Oklahoma, Inc.
  - Small Business Capital Corp.
  - Tulsa Economic Development Corp.

# Federal Small Business Lending

- SBA 504 Loan Program
- Provides loans to small businesses for fixed assets and M&E.
- Combination loan structure to mitigate risk of private lender by providing federal resources
  - 50% - Private lender
  - 40% - SBA loan
  - 10% - Borrower equity
- SBA portion is fully backed by SBA guarantee
- Many rules and regulations. Intended for small businesses but definition and limitations can be stretched.

# Access to Capital Tool Resources

- CDFA Resources:

  - Revolving Loan Fund (RLF) Resource Library

  - Intro Revolving Loan Fund Course, November 9-10, 2010
  - RLF Reference Guide (Nov. 2010)

# Practice Area 5:

# Support Tools

# Support Tools

- Incentives, federal & state funding, grants, etc. play a major support role in the financing toolbox.
- Tax abatements abound – nearly every state offers some form of abatement.
- Federal government currently operates over 30 support programs:

  - HUD, USDA, EDA, DOL, DOD, SBA, EPA, DOE, DOJ, Treasury, Interior, etc.

# Support Tools – A Few Programs

- HUD – CDBG, 108 Loan, BEDI
- EDA – Public Works, Economic Adjustment, Planning
- DOJ – Weed & Seed Grants
- DOD – BRAC Adjustment Grants
- SBA – 504 & 7(a) programs, many others
- Treasury – New Markets, Bank Enterprise
- National Science Foundation – SBIR/STTR
- Ex-Im Bank of U.S. – working capital loans

# Support Tools – A Few Programs

- DOL – Long-Term Care Training, Workforce Innovation in Regional Economic Development (WIRED) Initiative, High Growth Job Training Initiative
- EPA – Assessment Grants,Revolving Loan Fund Grants,Cleanup Grants, Job Training Grants, Brownfield Tax Credits
- USDA - Community facilities loans, grants & guarantees, broadband development loans, business loans, grants & guarantees, intermediary relending program, etc.

# Support Tool Resources

- CDFA Resources:

  - Federal Finance Guide (in development)
  - Federal Financing Resource Center (in development)

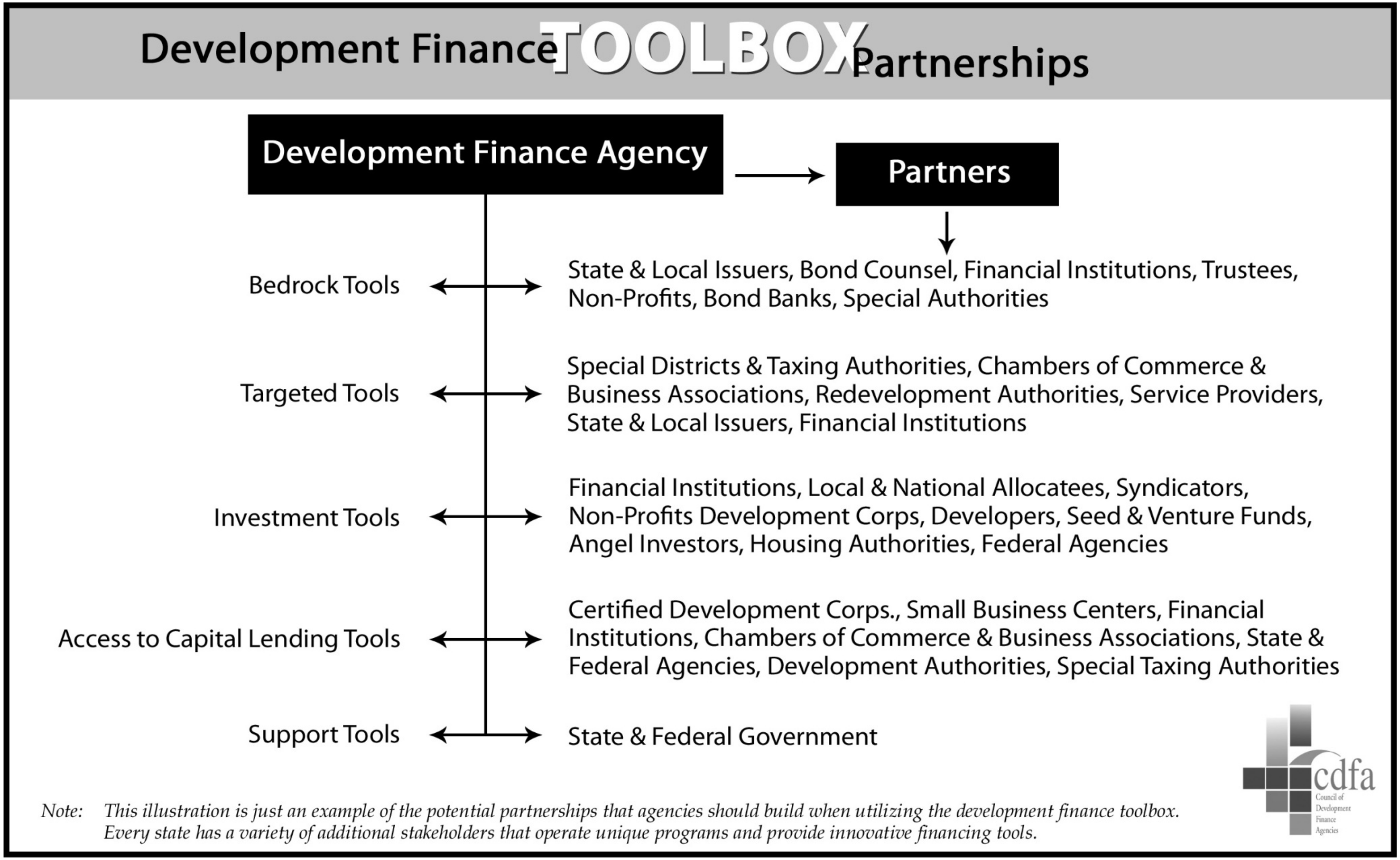
  - Federal Financing Course (early 2011)

# *Implementing the Development Finance Toolbox*

# Keys to Toolbox Success

- Comprehensive effort involving bold thinking, innovative planning, considerable strategizing and a fully supported, cooperative effort from all involved.
- Agencies that fail to build partnerships typically fail to implement the toolbox.
- Bring stakeholders to the table – don't try to operate all of these programs on your own.
- Partnerships should exist on the local, county, regional, state and federal level through the public, private, non-profit communities.

# Partnerships Matter



# Sharing Risk, Credit & Expenses

- Very few agencies are able or willing to accept all of the risks involved in the toolbox approach.
- Fewer have the resources or capacity to operate all of these programs.
- However, agencies within your community do have this capacity through their design and fee structures and should be part of the toolbox partnership (i.e. CDCs for the 504 program, etc.).

# Sharing Risk, Credit & Expenses

- The private sector should be considered a risk and credit sharing partner.
- Private sector is eager and willing to participate and they provide far greater depth of risk ability then other partners.
- State and federal laws mandate private investment (CRA). Use this to your toolbox advantage.
- Private sector also has the resources to absorb the expenses of running these programs and they will expect to earn a return.

# Operations & Structuring

- For larger agencies with more capacity, consider structuring your agencies like a business with divisions and experts in each area – business finance, development finance, etc.

- Consider a public/private model if community faces political/turf war challenges.

- Build and adequate fee structure – the private sector does, so why not the public agency?

# Implementing the Toolbox

- Create a ***Strategic Financing Plan*** that mirrors the community’s master plan and economic development strategy.
- Seek innovative strategies – think about industries not served by existing programs and create program that serve these needs.

# Implementing the Toolbox

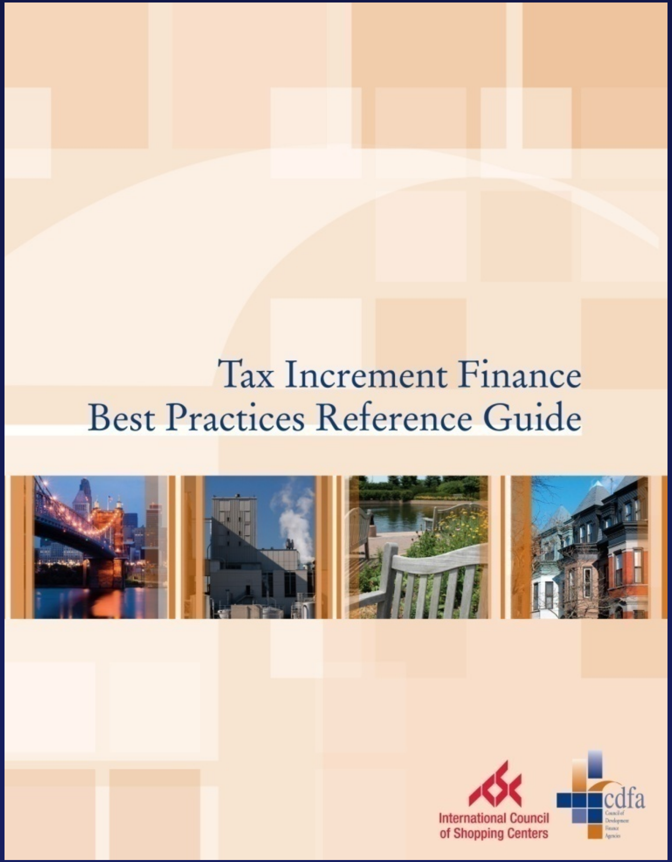
- Operate programs with performance based measuring in place. Track returns closely, be accountable, report findings and use the internet.
    - job creation, investment, taxes, blight removal, property values, population attraction, transformation, investment return, etc.
- Consider policy and procedures closely and engage in healthy dialogue to determine appropriate use of financing tools.
- Decide: Developer/business driven or community driven policy?

# Best Practices

- City of Minneapolis, MN
- Atlanta Development Authority, GA
- City/County of Denver, CO & Denver Urban Redevelopment Authority
- Allegheny County Economic Development, PA
- St. Louis County Economic Council, MO
- Chester County Economic Development Council, PA
- New Jersey Economic Development Authority
- MassDevelopment
- Arkansas Development Finance Authority
- Business Oregon

# CDFA Research & Resources

- CDFA website: www.cdfa.net
- Development Finance Review Weekly e-newsletter
- Online Resource Database
- Online Resource Libraries:
  - Bond Finance
  - Tax Credit Finance
  - Tax Increment Finance
  - Revolving Loan Funds



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