

Approved February 3, 1988
Date

MINUTES OF THE SENATE COMMITTEE ON ECONOMIC DEVELOPMENT

The meeting was called to order by Senator Wint Winter, Jr. at
Chairperson

12:30 ~~xxx~~/p.m. on January 28, 1988 in room 254-E of the Capitol.

All members were present except:

Senator Paul Burke - Excused Senator Alicia Salisbury - Excused
Senator Paul Feleciano - Excused
Senator Fred Kerr - Excused

Committee staff present:

Lynne Holt, Legislative Research Department
Bill Edds, Revisor of Statutes' Office
Mary Allen, Secretary to the Committee

Conferees appearing before the committee:

Senator Eugene Anderson, Kansas State Senate
Roland Smith, Executive Director of the Wichita Independent Business Association

The meeting was called to order by the Chairman, Senator Wint Winter, Jr. at
12:30 p.m..

Senate Bill 176 - An Act creating the small contractors and small businesses'
revolving loan fund.

Staff reviewed the history of SB 176 and noted that it was introduced by Senator Eugene Anderson during the 1987 Session of the Legislature. The Senate Economic Development Committee held a hearing on the bill and then referred it for interim study. Staff said that SB 176, as introduced, authorizes the establishment of a small contractors and small businesses' revolving loan fund. These companies, with gross revenues not exceeding \$500,000.00, must have been doing business and must have maintained their principal office in the state for at least one year prior to application for assistance. They must also be, or intend to be, located in an enterprise zone. The bill specifies that the total amount of a loan to any one business shall not exceed \$200,000.00 annually. The Secretary of Commerce would administer the revolving loan fund and develop rules and regulations in consultation with the state's small business development centers. Staff observed that during the 1987 Interim, the Joint Committee on Economic Development discussed the bill and noted in its report that a small business loan guarantee program would be preferable to a direct loan program in that a guarantee program would be less risky for the state and would increase the state's leveraging capacity.

Senator Eugene Anderson, sponsor of SB 176, appeared before the Committee in support of the bill. (See Attachment I for his statement.) He observed that it is probably a lot easier to borrow \$500,000.00 than it is to borrow \$50,000.00. He stated that the Small Business Administration (SBA) has a program of direct loans to small business people but they primarily target individuals who are Viet Nam veterans, especially those veterans who are handicapped. He pointed out that there is a group of people who cannot get initial money to start a business and that traditional lending institutions are not in the business of lending start-up funds. He said that there needs to be some mechanism at the state level to help those small business people who have difficulty gaining access to capital through lending institutions.

In answer to a question by Senator Karr, Senator Anderson stated that he would have no problem with the revolving loan fund in SB 176 being changed to a loan guarantee program and that the program should be administered through the Kansas Department of Commerce.

CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON ECONOMIC DEVELOPMENT

room 254-E, Statehouse, at 12:30 ~~xxx~~ p.m. on January 28, 1988

Senator Daniels expressed concern over the provision in SB 176 that the revolving loan fund would be limited to businesses in enterprise zones. Senator David Kerr asked Senator Anderson if he would object to eliminating the requirement in the bill that the business must be in an enterprise zone and to target the bill instead towards the business being a "primary industry". He pointed out that the Interim Committee on Economic Development proposed to define "primary industry" and to make almost all of the incentives provided to companies in the state targeted towards primary industries. He observed that the primary industry definition proposed would generally include industries which import capital and jobs into the state. He observed that, to a large extent, the definition proposed does not include retail businesses. Senator Anderson pointed out that a lot of small businesses are retail businesses. He said that he does not agree with the "primary industry" approach for he does not feel that the Legislature should put together any program which basically discriminates against retail businesses.

Roland Smith, Executive Director of the Wichita Independent Business Association, spoke in support of SB 176. Mr. Smith stated that his Association is constantly seeing small businesses left out of most economic development programs. He pointed out that eighty-two percent of the businesses in Kansas have twenty-five or less employees. He observed that the venture capitalists are not interested in this size business unless it is high tech with a high return and controlling ownership. Mr. Smith said that SB 176 is very welcome as it would meet a definite need which exists and which has been long ignored. (See Attachment II for his statement.)

Mr. Smith told the Committee that if the requirement of a business being located in an enterprise zone is left in SB 176, ninety percent of the businesses which he represents would be eliminated from the proposed loan program. He stated that he would have no problem with the bill being amended to change the revolving loan fund to a loan guarantee program. Mr. Smith observed that he does not agree with the "primary industry" concept. Senator Karr asked Mr. Smith for suggestions on the administration of a loan guarantee program. Mr. Smith said that he would like to see the loan applications begin in the Department of Commerce, then filter down to the Small Business Development Centers and finally to the Certified Development Companies.

Mr. Smith stated that the Small Business Administration (SBA) loans do not reach the vast majority of businesses in need because of the SBA's priorities and its limited money. Chairman Winter asked Mr. Smith to gather information for the Committee concerning identifying the existing gaps in the SBA's loan guarantee program.

Senator Karr moved that staff be directed to prepare a draft bill, for further Committee consideration, which would change the proposed revolving loan fund in SB 176 to a loan guarantee program. He further moved that staff should identify policy questions in the draft and suggest various options to those questions. Senator Vidricksen seconded the motion. The motion carried.

The Chairman asked staff to work with Senator Anderson and the Ranking Minority Member, the Vice-Chairman and the Chairman of the Committee in preparing this bill draft.

Senator Daniels moved to remove the limitation that businesses must be located in an enterprise zone from the proposed bill to be drafted by staff. Senator Vidricksen seconded the motion. The motion carried.

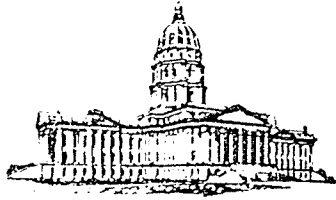
The meeting was adjourned at 1:30 p.m. by the Chairman.

GUEST LIST

NAMEREPRESENTING

Tony Augusth	Dept. of Commerce
JACK MONTGOMERY	KDOC
Robert E. Smith	WIBA
Nancy McCabe	KDOC
Stan McAdoo	KDOC
Wayne ZIMMERMAN	KDOC
Eugene Anderson	Senate
Gina Sanborn	IPPBR - K.U.

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TOPEKA

SENATE CHAMBER

COMMITTEE ASSIGNMENTS
MEMBER CONFIRMATIONS
EDUCATION
PUBLIC HEALTH AND WELFARE
RANKING MINORITY MEMBER FEDERAL AND STATE
AFFAIRS

TO; THE CHAIRMAN-MEMBERS OF THE COMMITTEE

WE ARE MOST APPRECIATIVE OF THE TIME YOU HAVE ALLOWED FOR PROponents OF THIS BILL, SENATE BILL 176, WHICH PROVIDES FOR THE ESTABLISHMENT OF A REVOLVING LOAN FUND TO BE ESTABLISHED TO ASSIST, SMALL BUSINESSES AND SMALL CONTRACTORS, WITH LIMITED FINANCIAL ASSISTANCE. HOWEVER, SUCH FINANCIAL ASSISTANCE WILL BE RESTRICTED TO SMALL BUSINESS AND SMALL CONTRACTOR LOCATED OR THAT AGREE TO LOCATE OR EXPAND IN AREAS HAVING BEEN IDENTIFIED AS "ENTERPRISE ZONES".

APPROXIMATELY 98 PERCENT OF ALL AMERICAN BUSINESSES ARE "SMALL". ONLY 10,000 OF THE NATION'S BUSINESSES HAVE 500 OR MORE EMPLOYEES. SMALL BUSINESS EMPLOYS 47 PERCENT OF THE NON-GOVERNMENTAL LABOR FORCE.

ALMOST 80 PERCENT OF ALL NET JOBS COME FROM FIRMS WITH FEWER THAN 100 EMPLOYEES, ACCORDING TO RESEARCH DONE AT MICHIGAN INSTITUTE OF TECHNOLOGY, BETWEEN 1969 AND 1976, AND TWO-THIRDS OF ALL NEW JOBS ARE ACCOUNTED FOR BY FIRMS WITH 20 OR FEWER EMPLOYEES. FUTUREMORE, IN THE NORTHEAST SMALL BUSINESS JOB GAINS MADE UP FOR OPPORTUNITIES LOST BY THE LARGEST CORPORATIONS DURING THE SAME PERIOD.

Attachment I
Senate Eco Dev
1-28-88

IN ADDITION, NATIONAL SCIENCE FOUNDATION AND COMMERCE DEPARTMENT REPORTS CONCLUDED THAT SMALL BUSINESS WAS "24" TIMES MORE INNOVATIVE PER RESEARCH AND DEVELOPMENT DOLLAR THAN LARGE FIRMS." THUS, CONTRARY TO POPULAR BELIEF, A STATE'S JOB CREATION, EVEN IN THE FARM BELT STATES, WILL COME FROM FOSTERING LOCAL BUSINESSES, NOT FROM ATTRACTING BUSINESS FROM OUT OF STATE.

YET FOR SMALL BUSINESS, LACK OF ACCESS TO CAPITAL IS A MAJOR PROBLEM, AND THE ECONOMIC RECESSION HAS SEVERELY MAGNIFIED THIS PROBLEM. THE RATE OF BUSINESS FAILURES IN 1982 AND 1983 RAN FIVE TIMES AHEAD OF THE RATE IN 1981.

MOST SMALL BUSINESSES FINANCE THEIR WORKING CAPITAL WITH SHORT TERM, BANK-FINANCED DEBT. THE OVRATING INCREASES IN THE INTEREST RATES HAVE SEVERELY STRAINED THE DEBT-SERVICE CAPABILITIES OF MOST SMALL BUSINESSES. WITHOUT THE INTERNAL RESERVES TO WITHSTAND THE LONG PERIOD OF HIGH RATES, AND WITHOUT AN ABILITY TO FULLY PASS ALONG THESE INCREASED "COSTS" OF DOING BUSINESS TO THEIR CUSTOMERS, SMALL BUSINESSES ARE FORCED TO CLOSE THEIR DOORS. THE FARM SECTOR, COMPRISED MOSTLY OF SMALL BUSINESSES, HAS ALSO EXPERIENCED A STEEP ECONOMIC DECLINE.

SINCE APPROXIMATELY 80 PERCENT OF SMALL BUSINESSES RELY ON FINANCING FROM DESPOSITORY INSTITUTIONS, AN INCREASE IN THE COST OF FINANCING AND A DECREASE IN THE AVAILABILITY OF FUNDS HAS A MORE SEVERE IMPACT ON SMALLER FIRMS THAN ON LARGER FIRMS.

THE SMALL BUSINESS ADMINISTRATION'S DIRECT LOAN AND LOAN GUARANTEE PROGRAMS HAVE HELPED, BUT ARE BEING REDUCED. IN FACT, THE SBA PROGRAM IS A VERY MODEST CAPITAL CORRECTING MECHANISM THAT NEEDS EXPANSION TO COUNTER THE GOVERNMENT'S CAPITAL MARKET INTERFERENCE.

THERE IS SOME CONTROVERSY OVER WHETHER CAPITAL ACCESS IS THE MOST IMPORTANT PROBLEM OR WHETHER THE COST OF CAPITAL IS MORE IMPORTANT. BOTH ARE IMPORTANT, BUT SOME CAPITAL ACCESS PROBLEMS CAN BE SOLVED THROUGH MODEST AND INEXPENSIVE MARKET RESTRUCTURING. SUCH AS THE ESTABLISHMENT OF A REVOLVING LOAN FUND TO ASSIST SMALL BUSINESSES AND SMALL CONTRACTORS.

THE NEW PUBLIC POLICIES BEING PROPOSED FOR SMALL BUSINESSES ARE BASICALLY ORIENTED TOWARD IMPROVING CAPITAL ACCESS, NOT REDUCING THE CAPITAL COST. THIS WILL HELP MANY BUSINESSES AT LITTLE OR NO GOVERNMENT COST, BUT WILL NOT SOLVE THE PROBLEM FOR OTHER BUSINESSES THAT REQUIRE CAPITAL TO SURVIVE OR EXPAND.

THIS PROGRAM PROPOSAL SHOULD NOT AIM EXCLUSIVELY TO SATISFY A SMALL BUSINESS CONSTITUENCY, BUT TO CREATE A CLIMATE OF ECONOMIC AND JOB GROWTH. THE POTENTIAL ENTREPRENEUR AND THE STRUGGLING, GROWING COMPANY -- NOT MATURE SMALL BUSINESSES MORE INTERESTED IN PROTECTING THEIR GAINS -- SHOULD BE TARGETED FOR AID. THE GOAL OF MAKING FINANCIAL INSTITUTIONS MORE RESPONSIVE TO THE NEEDS OF SMALL BUSINESSES WILL BE WELL RECEIVED, BUT SPECIFIC PROGRAM PROPOSALS SHOULD EXTEND BEYOND THE INTERESTS OF THE

ORGANIZED SMALL BUSINESS POLITICAL CONSTITUENCIES. THEREFORE, NEW PUBLIC POLICIES SHOULD BE PURSUED AS PART OF AN OVERALL STRATEGY OF ECONOMIC GROWTH, NOT AS A SMALL BUSINESS CONSTITUENCY ISSUE.

ON THE WHOLE, SMALL BUSINESSES APPEAR TO BE AS PROFITABLE, IF NOT MORE, THAN LARGE CORPORATIONS. BETWEEN 1972 AND 1976, U.S. MANUFACTURING CORPORATION WITH ASSETS UNDER \$1 BILLION RETURNED ONLY 12.91 PERCENT, ACCORDING TO THE FEDERAL TRADE COMMISSION.

BIASES IN FEDERAL POLICIES HAVE TRADITIONALLY GIVEN FIRMS AN INCENTIVE TO INVEST OUTSIDE OLDER AMERICAN CITIES AND OUTSIDE LOWER-INCOME URBAN AREAS. THE CAPITAL MARKETS ALLOW BIG BUSINESS BETTER ACCESS TO FINANCING THAN NEW, YOUNG AND SMALL FIRMS.

SMALL AND YOUNG COMPANIES EXPLORE NEW AVENUES AND NEW COMBINATIONS OF RESOURCES MORE EASILY, MORE CREATIVELY, AND LESS RISK THAN LARGE INSTITUTIONS. SMALL COMPANIES ARE PARTICULARLY IMPORTANT SOURCES OF LOCAL ECONOMIC VITALITY IN TERMS OF JOB CREATION, PROFITABILITY, TECHNOLOGICAL INNOVATION, AND EQUAL OPPORTUNITY.

IN CLOSING WE WOULD LIKE TO OUTLINE SOME APPROACHES TO ASSIST SMALL BUSINESSES AND SMALL CONTRACTORS.

FIRST, THE SKILLS OF ENTREPRENEURS, BOTH IN PRIVATE AND

COMMUNITY-BASED-VENTURES, NEED TO BE ENHANCED BY BETTER-COORDINATED EDUCATION, TRAINING AND TECHNICAL ASSISTANCE SERVICES. SUCH SERVICES COULD BE PROVIDED BY THE KANSAS DEPARTMENT OF ECONOMIC DEVELOPMENT, SPECIFICALLY THE MINORITY BUSINESS DIVISION. FOR EXAMPLE, THE EMPLOYMENT PLACEMENT AND TRAINING PARTNERSHIP ACT, COULD BE USED TO HELP THE UNEMPLOYED BECOME NEW BUSINESS OWNERS. THE SUCCESSFUL BE-YOUR-OWN-BOSS PROGRAM IN BROWARD COUNTY, FLORIDA, ARRANGED LOANS FROM SEVEN LOCAL BANKS AND TRAINED CETA-ELIGIBLES TO ESTABLISH 44 NEW BUSINESSES. ANOTHER STRATEGY IS THE CREATION OF TECHNICAL ASSISTANCE OFFICES LIKE THE MASSACHUSETTS COMMUNITY ECONOMIC DEVELOPMENT ORGANIZATIONS STARTING OR EXPANDING BUSINESSES.

SECOND, HIGHER COSTS OF PRODUCTION DISCOURAGE FIRM START-UP, EXPANSION, AND RELOCATION IN MANY COMMUNITIES. THE COSTS OF LAND AND TAXES CAN ALL BE ADDRESSED BY APPROPRIATE PUBLIC POLICIES. "LAND BANKS" HAVE BEEN ESTABLISHED IN CLEVELAND, PHILADELPHIA AND MILWAUKEE TO ACQUIRE AND IMPROVE CONTIGUOUS PARCELS OF LAND. LOCAL GOVERNMENTS SHOULD USE THE URBAN IDENTIFICATION SYSTEM DEVISED BY THE COUNCIL ON NORTHEAST ACTIONS TO DETERMINE WHAT BUSINESSES ARE UNDER REPRESENTED IN THEIR COMMUNITIES. SUCH RESEARCH WILL HELP NEIGHBORHOOD GROUPS, SMALL BUSINESSPERSONS AND LENDERS IDENTIFY PROMISING BUSINESS VENTURES.

LOCAL CITIZENS ORGANIZATIONS ARE ALSO A LARGELY UNTAPPED SOURCE OF ENTRENEURSHIP. BALTIMORE, PHILADELPHIA, KANSAS CITY, MISSOURI, NEW YORK CITY AND SAN DIEGO HAVE AIDED NEIGHBORHOOD

GROUPS IN ESTABLISHING BUSINESSES FOR DELIVERING LOCAL SERVICES. URBAN DEVELOPMENT ASSISTANCE GRANTS AND COMMUNITY DEVELOPMENT BLOCK GRANT MONIES CAN BE USED FOR ENTREPRENEURIAL FINANCE, AS NEW YORK CITY HAS DONE. LOCAL GOVERNMENTS COULD ALSO EXPLORE USING COMMUNITY DEVELOPMENT BLOCK GRANT MONIES TO GUARANTEE INDUSTRIAL REVENUE BONDS FOR FIRMS MEETING CERTAIN TESTS OF SIZE AND LOCATION.

NEW ENTERPRISE DEVELOPEMENT AS A REVITALIZATION STRATEGY IS NOT, OF COURSE WITHOUT PROBLEMS. THE QUALITY OF JOBS PRODUCED INTERMS OF WAGE LEVELS, FRINGE BENEFITS AND LOGEVITY IS OFTEN LOWER THAN AVERAGE. THE CLOSURE RATE OF SMALL BUSINESS IS VERY HIGH; MORE THAN 60 PERCENT OF NEW FIRMS DO NOT SEE THEIR FIFTH BIRTHDAY, ALTHOUGH LESS THAN ONE PERCENT OF NEW BUSINESSES FAIL WITH LOSS TO CREDITORS.

THE STATE SHOULD REQUIRE FINANCIAL REGULATORS, IN THEIR ANNUAL REPORT TO THE GOVERNOR AND LEGISLATURE, TO REPORT ON THE PERFORMANCE OF THE INSTITUTIONS IN SUPORTING PRODUCTIVE BUSINESS DEVELOPMENT.

THE STATE SHOULD DEVELOP A STATE-LEVEL EQUIVALENT OF THE 1977 FEDERAL COMMUNITY REINVESTMENT ACT, WHICH DIRECTED REGULATORS TO CONSIDER WHETHER BANKS WERE MEETING THE NEEDS OF THE COMMUNITY. SUCH AN ACT SHOULD FOCUS ON A BANK'S RECORD IN MEETING THE NEEDS OF SMALL BUSINESS AS WELL AS CONSUMERS AND MORTGAGE LOANS.

THE STATE SHOULD INSURE THAT SMALL BUSINESSES ARE REPRESENTED ON THE BOARDS OF DIRECTORS OF MAJOR FINANCIAL INSTITUTIONS. MAJOR BANKS SELDOM HAVE SMALL BUSINESS REPRESENTATION.

THE STATE SHOULD ESTABLISH LOAN LOSS RESERVE PROGRAMS. THESE PROGRAMS DEVELOP A SPECIAL RESERVE FUND TO ALLOW BANKS TO MAKE LOANS OF MORE THAN NORMAL RISK. THEY WORK BEST IN STATES THAT HAVE A SUBSTANTIAL PERCENTAGE OF BANKING ASSETS IN LARGE BANKS, SINCE THE PROGRAM REQUIRES EACH PARTICIPATING BANK TO DEVELOP A LOSS RESERVE COVERING A BROAD PORTFOLIO OF LOANS.

THE STATE SHOULD CREATE A NEW CLASS OF COMMERCIAL LENDERS TO PROVIDE FUNDS FOR VENTURE CAPITAL FIRMS. CALIFORNIA, NEVADA AND SOME OTHER STATES HAVE CREATED "BUSINESS AND INDUSTRIAL DEVELOPMENT CORPORATIONS" (BIDCOs) TO GENERATE MORE SOPHISTICATED FINANCING FOR VENTURE CAPITAL COMPANIES. THESE INSTITUTIONS MAKE GOVERNMENT GUARANTEED LOANS AND SELL THE GUARANTEES TO LEVERAGE THEIR FUNDS. SINCE THEY DO NOT TAKE DEPOSITS AND DO NOT HAVE FIDUCIARY RESPONSIBILITY OR FEDERAL INSURANCE, THEY CAN TAKE EQUITY POSITION AND DEVELOP MUCH MORE FLEXIBLE FINANCING RESPONSES THAN IS THE CASE FOR BANKS.

JANUARY 28, 1988

STATEMENT TO; SENATE ECONOMIC DEVELOPMENT COMMITTEE
SUBJECT; SENATE BILL 176
FROM; ROLAND SMITH, EXECUTIVE DIRECTOR OF THE WICHITA
INDEPENDENT BUSINESS ASSOCIATION.

I AM ROLAND SMITH, EXECUTIVE DIRECTOR OF THE WICHITA INDEPENDENT BUSINESS ASSOCIATION. WIBA IS AN ASSOCIATION OF OVER 1400 LOCALLY OWNED BUSINESSES IN THE WICHITA, SEDGWICK COUNTY AREA. OVER 1200 OF THESE BUSINESSES HAVE 5 OR LESS EMPLOYEES. OUR ASSOCIATION ENCOMPASSES 352 DIFFERENT TYPES OF BUSINESSES.

WE ARE CONSTANTLY SEEING THE SMALL BUSINESSES THE SIZE WE REPRESENT LEFT OUT OF MOST ECONOMIC DEVELOPMENT PROGRAMS BE IT CITY, COUNTY OR STATE. JUST LAST TUESDAY THE WICHITA CITY COUNCIL LIMITED THE NEW TAX ABATEMENT POLICY OF THE CONSTITUTIONAL AMENDMENT TO NEW BUSINESSES WITH MORE THAN 5 EMPLOYEES. 82% OF THE BUSINESSES IN KANSAS HAVE 25 OR LESS EMPLOYEES. THE VENTURE CAPITALIST ARE NOT INTERESTED IN THIS AREA UNLESS IT IS HIGH TECH WITH A HIGH RETURN AND CONTROLLING OWNERSHIP. IF YOU GO TO A BANK YOUR STATEMENT HAS TO BE SO GOOD YOU DON'T REALLY NEED A LOAN. THERE ARE LOANS AVAILABLE FOR CAPITAL INVESTMENTS AND VERTUALLY NONE FOR WORKING CAPITAL. FOR THE MOST PART BUSINESS DOES NOT LIKE TO SEE MORE GOVERNMENT INVOLVEMENT, BUT THE FACT OF LIFE IS THAT THE SMALL INDEPENDENT

*Attachment II
Senate Eco D evr
1-28-88*

BUSINESS WHICH IS THE CORE OF OUR DEMOCRACY IS RAPIDLY BEING SQUEEZED OUT. EVERYONE IS CRYING ABOUT THE FAMILY FARM GOING DOWN THE TUBE, BUT I DON'T HEAR ANYONE CRYING OUT ABOUT THE FAMILY BUSINESS. THE COMMON REMARK IS THAT'S TOUGH! ITS' THE FREE ENTERPRISE SYSTEM.

THIS BILL IS VERY WELCOME AS IT WILL MEET A DEFINITE NEED THAT EXISTS OUT THERE THAT HAS BEEN LONG IGNORED. THERE HAS BEEN A LOT OF TALK ON ECONOMIC DEVELOPMENT AND LITTLE ACTION IN THE AREAS WHERE THE MOST GROWTH ACTUALLY COMES FROM.

IF YOU HAVE ANY QUESTIONS, I'LL BE GLAD TO ANSWER IF I CAN.