

Return-on-Investment of the Florida Microfinance Loan and Microfinance Guarantee Programs

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EXECUTIVE SUMMARY

Background and Purpose

Legislation enacted in 2014 directs the Office of Economic and Demographic Research (EDR) to analyze and evaluate the first 3 years of the Microfinance Loan Program and the Microfinance Guarantee Program.¹ These programs are intended to expand job opportunities for the state's workforce by expanding access to credit for entrepreneurs and small businesses.²

EDR is required to evaluate the economic benefits of each program, the number of jobs created, the increase or decrease in personal income, and the impact on state gross domestic product from the direct, indirect, and induced effects of the state's investment. Economic Benefit is defined as "the direct, indirect, and induced gains in state revenues as a percentage of the state's investment" – which includes "state grants, tax exemptions, tax refunds, tax credits, and other state incentives."³ For the purpose of this report, the term Return on Investment (ROI) is synonymous with economic benefit, and is used in lieu of the statutory term.

EDR is also directed to identify any inefficiencies in the programs and provide recommendations for changes to the programs.

Explanation of Return-on-Investment

The ROI is developed by summing state revenues generated by a program less state expenditures invested in the program, and dividing that calculation by the state's investment. It is most often used when a project is to be evaluated strictly on a monetary basis, and externalities and social costs and benefits—to the extent they exist—are excluded from the evaluation. The basic formula is:

$$\frac{(\text{Increase in State Revenue} - \text{State Investment})}{\text{State Investment}}$$

Since EDR's Statewide Model is used to develop these computations and to model the induced and indirect effects, EDR is able to simultaneously generate State Revenue and State Investment from the model so all feedback effects mirror reality. The result (a net number) is used in the final ROI calculation.

As used by EDR for this analysis, the returns can be categorized as follows:

- **Greater Than One (>1.0)**...the program more than breaks even; the return to the state produces more revenues than the total cost of the investment.
- **Equal To One (=1.0)**...the program breaks even; the return to the state in additional revenues equals the total cost of the investment.
- **Less Than One, But Positive (+, <1)**...the program does not break even; however, the state generates enough revenues to recover a portion of its cost of the investment.
- **Less Than Zero (-, <0)**...the program does not recover any portion of the investment cost, and state revenues are less than they would have been in the absence of the program, typically because taxable activity is shifted to non-taxable activity.

¹ Section 55, ch. 2014-218, L.O.F., creating s. 288.9937, F.S.

² Section 288.9931, F.S.

³ Section 288.005(1), F.S.

The numerical ROI can be interpreted as the return in tax revenues for each dollar spent by the state. For example, a ROI of 2.5 means that \$2.50 in tax revenues is received back from each dollar spent by the state.

The basic formula for ROI is always calculated in the same manner, but the inputs used in the calculation can differ depending on the needs of the investor. Florida law requires the return to be measured from the state's perspective as the investor, in the form of state tax revenues. In this regard, the ROI is ultimately shaped by the state's tax code.

Results and Conclusions

The Microfinance Loan Program and Microfinance Guarantee Programs supplement or complement existing programs, providing capital to enable them to expand services (loans and loan guarantees) to qualified borrowers in the target market.⁴

Through third-party program administrators, the **Microfinance Loan Program** provides funding of up to fifty percent of fixed-rate, short-term loans, not to exceed \$50,000, to qualified Florida businesses with 25 employees or fewer and gross annual revenues of \$1.5 million or less per year for the last 2 years. As a condition of receiving the loan, the borrower must participate in business management training through the network of Florida Small Business Development Centers (SBDCN Centers). Through FY 2016-17, \$1,345,407 in state funds (26.25 percent of the \$5,125,000 total allocation) has been loaned to businesses through the Loan Program.

Through Enterprise Florida, Inc. (EFI), the **Microfinance Guarantee Program** backs loans by private lenders to Florida businesses. Like the microloan program, eligibility is limited to businesses with 25 employees or fewer and gross annual revenues of \$1.5 million or less per year for the last 2 years. Guarantees are limited to loans of \$50,000 to \$250,000, and may range from 25 to 50 percent of the total loan amount. Through FY 2016-17, \$841,639 (17.4 percent of the \$4,825,000 total allocation) has been used to support loans to businesses through the Guarantee program.

This review shows the state's ROI for the loan program is 0.15, and 0.08 for the Loan Guarantee program. A significant factor behind these ROIs is the large amount of activity that had to be culled because of market dependency.

While the returns associated with these programs are low, some points are worth noting. First, the primary factors that drive ROI are job creation and capital investment associated with construction, renovation and purchase of equipment. With a few exceptions, loans funded through these programs do not create high-wage jobs in high performing industries. Similarly, they are not typically associated with major capital investments.⁵

Second, this analysis captures the impact of a new, fully-funded program whose implementation was delayed – six months for the loan program and one year for the guarantee program. Also, for the loan program there was significantly more activity in the third year than in the previous two and one-half

⁴ For an overview of other state-supported financial and technical assistance programs for small businesses, as well as venture capital programs for startup businesses, see APPENDIX Two.

⁵ For a discussion of other factors affecting ROI, see EDR's PowerPoint Presentation "Return on Investment in Florida Practice" http://edr.state.fl.us/Content/returnoninvestment/ROI_InFloridaPractice.pdf

years, indicating greater use as the program matures. The ROI should improve over time as repaid loans are recycled (should the program be continued) and as unobligated guarantees are re-invested and maintained as a recurring source of program funding.⁶

Third, a return on investment is a measure of financial returns and does not address issues of overall effectiveness or societal benefit. The stated purpose of the Microfinance Loan and Guarantee programs is to increase access to credit for entrepreneurs and small businesses in Florida. It may be beneficial to the state if access to credit and business management training promotes a more stable and productive small business sector, even if the financial returns to the state are initially minimal.

Fourth, these programs are not designed and administered like an economic development program. Program administrators are not required to screen projects for Florida market or resource dependency or evaluate projects for the ROI to the state as DEO does for state economic development incentives.⁷ Indeed, most of the businesses assisted through the Microfinancing programs are Florida market dependent. While expanding “job opportunities for this state’s workforce” is an expressed intent of these programs,⁸ they are not conditions for receipt of a loan or loan guarantee.

Finally, the low ROIs were significantly related to funding the entire combined program upfront coupled with the long implementation delay. This means that 100 percent of the cost is reflected in the ROI, with only 22 percent returned to the economy. The remaining 78 percent of funds were retained and not put to productive economic use. The ROIs would have been higher had the retained amount been released as loans and guarantees.

Other than this, EDR’s review of the Microfinance Loan and Guarantee programs show they are an efficient means to meet program goals. First, the programs “avoid duplicating existing programs”⁹ by targeting small loans that were unaddressed by existing programs. Second, almost all of the initial (and to date, only) state appropriation for these programs is preserved, as deductions for administrative expenses are statutorily capped or prohibited. Further, program funds are required to be reinvested and maintained as a recurring source of program funding. These program design features contribute to the efficient implementation and continued cost-efficiency of the Microfinance programs.

Recommendation

If the Legislature intends the Microfinance Loan program to operate beyond 2017, it should clarify that the principal from repaid loans recovered by DEO at the termination of its contract with the loan administrators be reallocated to the current or newly-qualified loan administrators.

The Legislature should also consider focusing the programs on entrepreneurship by targeting only businesses with innovations that satisfy a specific need or result in revolutionary products. The program criteria would otherwise remain the same. This recommendation is based on information contained in Appendices One and Two, as well as an attempt to cure some of the market dependency. Perhaps with a more limited focus, DEO would have better success in marketing the program.

⁶ While s. 288.9934(4)(a), F.S., infers the loan program will “be maintained as a long-term and stable source of funding for the program,” paragraph (3)(a) does not specifically authorize a subsequent round of awards to program administrators at the end of the initial three-year contracts.

⁷ For an overview of all incentive programs administered through DEO, see The DEO/EFI 2016 Incentives Report @ <http://www.floridajobs.org/docs/default-source/reports-and-legislation/final-version-incentives-report.pdf?sfvrsn=4>

⁸ Section 288.9931, F.S.

⁹ Section 288.9931, F.S.

OVERVIEW OF FLORIDA'S MICROFINANCE LOAN AND MICROFINANCE GUARANTEE PROGRAMS

In 2014, the Florida Legislature enacted the “Florida Microfinance Act,”¹⁰ which created two programs through the Department of Economic Opportunity (DEO) to increase access to credit for entrepreneurs and small businesses in Florida: the Microfinance Loan and Microfinance Guarantee programs.¹¹ These two programs received \$10 million in nonrecurring funds in 2014, with authority to spend up to \$100,000 for marketing and promotion.¹² Appropriated funds are intended to be reinvested and maintained as a long-term and stable source of funding for these programs.¹³

The **Microfinance Loan Program**¹⁴ was designed:

“... to make short-term, fixed-rate microloans in conjunction with business management training, business development training, and technical assistance to entrepreneurs and newly established or growing small businesses for startup costs, working capital, and the acquisition of materials, supplies, furniture, fixtures, and equipment. Participation in the loan program is intended to enable entrepreneurs and small businesses to access private financing upon completing the loan program.”¹⁵

The law requires DEO to contract with one to three entities to administer the program. The program provides funding of up to fifty percent of fixed-rate, short-term loans (one year or less), not to exceed \$50,000, to qualified Florida businesses with 25 employees or fewer and gross annual revenues of \$1.5 million or less per year for the last 2 years. Loan administrators are also required to reserve ten percent of the program funds for businesses that employ less than six people and generated annual gross revenues of less than \$250,000 per year for the last 2 years. A borrower is limited to no more than two microloans per year, not to exceed a total of \$75,000, and no more than five microloans in any 3-year period.¹⁶ Loans are only available for startup costs, working capital, and the acquisition of materials, supplies, furniture, fixtures, and equipment.¹⁷ Loans are capped at the current prime rate plus 1000 basis points.¹⁸ As a condition of receiving the loan, the borrower “must participate in business management training, business development training, and technical assistance,” as determined by the

¹⁰ Sections 49 - 57, ch. 2014-218, L.O.F.

For an overview of two previously state-capitalized microfinance programs, see
<http://www.oppaga.state.fl.us/MonitorDocs/Reports/pdf/0677rpt.pdf>

¹¹ In the U.S., loans of \$50,000 or less to businesses with five or fewer employers are typically considered microloans. For an overview of microfinancing in the U.S. and the developing world, see APPENDIX One.

¹² Section 57, ch. 2014-218, L.O.F. \$5,125,000 was allocated to the Loan program and \$4,825,000 was allocated to the Guarantee program.

¹³ Sections s. 288.9934(4)(a) and 288.9935(1), F.S.

¹⁴ Section 52, ch. 2014-218, L.O.F. Section 288.9934, F.S. Also see <http://www.floridajobs.org/business-growth-and-partnerships/for-businesses-and-entrepreneurs/business-resources/florida-microfinance-program>; <http://www.floridajobs.org/docs/default-source/reports-and-legislation/2017-deo-annual-report.pdf?sfvrsn=2> p. 19; and <http://www.floridajobs.org/docs/default-source/reports-and-legislation/microfinanceannualreportfy16-17.pdf?sfvrsn=2>

¹⁵ Section 288.9934(1), F.S.

¹⁶ Section 288.9934(9)(d), F.S. The effective cap for a three-year period would be \$200,000.

¹⁷ Section 288.9934(9)(b), F.S., imposes specific restrictions on use of loan proceeds.

¹⁸ Section 288.9934(9)(d)6., F.S. On May 31, 2017, the capped interest rate was 14 percent. Loan administrators report loan interest rates from 13.25 to 14 percent.

loan administrator, through the network of Florida Small Business Development Centers (SBDCN Centers).¹⁹

Two entities are under three-year contracts to administer the Loan program: the Florida Black Business Support Corporation (\$300,000 allocation) and OUR MicroLending, LLC (\$4,825,000 allocation).²⁰ To date, a total of \$1,345,407 in state funds (26.25 percent of the combined \$5,125,000 allocation) has been loaned to businesses through the Loan Program. At the termination of the contracts, the loan administrators are required to remit the state portion of the principal from all repaid loans to DEO.²¹

The purpose of the **Microfinance Guarantee Program** is to “stimulate access to credit for entrepreneurs and small businesses in this state by providing targeted guarantees to loans made to such entrepreneurs and small businesses.”²² The program backs loans by private lenders to Florida businesses. Like the microloan program, access is limited to businesses with 25 employees or fewer and gross annual revenues of \$1.5 million or less per year for the last 2 years. Guarantees are limited to loans of \$50,000 to \$250,000, and may range from 25 to 50 percent of the total loan amount.²³

As required by law, DEO contracts with Enterprise Florida, Inc. (EFI) to administer the Guarantee program. To date, \$841,639 (17.4 percent of the \$4,825,000 allocation) has been used to support loans to businesses through the Guarantee program.

The Microfinance Loan and Guarantee programs are similar to the federally-funded State Small Business Credit Initiative (SSBCI) programs administered by DEO and EFI, except that the SSBCI programs have “a stated minimum loan size of \$250,000 and as such, tend to complement rather than compete with the Microfinance Programs.”²⁴

The Guarantee program (as well as the SSBCI funded Florida Loan Support and Florida Capital Access programs) are similar to the Florida New Markets Development Program (NMDP), in that state funds are used to leverage loans to businesses that might not otherwise qualify for loan. A major difference is that the state’s investment in the Guarantee program is fully recouped at the end of the loan term,

¹⁹ DEO reports that the SBDCN uses “Profit Mastery,” a training and technical assistance curriculum which includes six modules and provides applicants with financial literacy skills and business management training necessary for small business success. The Florida SBDCN provides entrepreneurial and business development services in 46 communities throughout the state. See <http://floridasbdc.org/Main.php> for additional information.

²⁰ The Florida Black Business Support Corporation dba Access Florida Finance Corporation provides financing to Florida’s small business owners. <http://www.accessfloridafinance.com/microfinance-loan-program/>

OUR Microlending is a Community Development Financial Institution that offers an alternative financial service for entrepreneurs whose needs are not met by regular banking institutions. <http://ourmicrolending.com/>

²¹ Section 288.9934(6)(a), F.S. While s. 288.9934(4)(a), F.S., infers the loan program will “be maintained as a long-term and stable source of funding for the program,” (3)(a) does not specifically authorize a subsequent round of awards to program administrators at the end of the initial three-year contracts.

See s. 288.006, F.S., for general parameters regarding loan programs administered by DEO.

²² Section 53, ch. 2014-218, L.O.F. Section 288.9935, F.S. <http://www.floridajobs.org/business-growth-and-partnerships/for-businesses-and-entrepreneurs/business-resources/florida-microfinance-program> and <http://www.floridajobs.org/docs/default-source/reports-and-legislation/microfinanceannualreportfy16-17.pdf?sfvrsn=2>

²³ A loan-to-state guarantee of 1:1, not to exceed 3:1. *See* s. 288.9935(3)(b) & (4), F.S. and Exhibit A, p. 2 @ <http://www.floridajobs.org/docs/default-source/reports-and-legislation/microfinanceannualreport15-16.pdf?sfvrsn=2>

EFI reports a 1:1 ratio of on guarantees to date.

²⁴ Microfinance Programs Annual Report, 2017. Division of Community Development, Florida Department of Economic Opportunity, November 1, 2017, p. 3. <http://www.floridajobs.org/docs/default-source/reports-and-legislation/microfinanceannualreportfy16-17.pdf?sfvrsn=2>

whereas the funds generated from the sale of tax credits for the NMDP are either retained by the intermediary or the borrower.²⁵

For an overview of other state-supported financial and technical assistance programs for small businesses, as well as venture capital programs for startup businesses, see APPENDIX Two.

²⁵ For EDR's 2016 evaluation of the Florida New Markets Development Program, see <http://edr.state.fl.us/Content/returnoninvestment/ROISELECTPROGRAMS2017final.pdf>

METHODOLOGY

Statewide Model

EDR is tasked with evaluating the economic benefits of the Florida Microfinance Loan Program and the Microfinance Guarantee Program, the number of jobs created, the increase or decrease in personal income, and the impact on state gross domestic product from the direct, indirect, and induced effects of the state's investment. Economic Benefit is defined as "the direct, indirect, and induced gains in state revenues as a percentage of the state's investment" – which includes "state grants, tax exemptions, tax refunds, tax credits, and other state incentives."²⁶ In this report, the term Return-on-Investment (ROI) is synonymous with economic benefit, and is used in lieu of the statutory term. This measure does not address issues of overall effectiveness or societal benefit; instead, it focuses on tangible financial gains or losses to state revenues, and is ultimately conditioned by the state's tax policy.

EDR used the Statewide Model to estimate the ROI for these programs. The Statewide Model is a dynamic computable general equilibrium (CGE) model that simulates Florida's economy and government finances.²⁷ The Statewide Model is enhanced and adjusted each year to reliably and accurately model Florida's economy. These enhancements include updating the base year the model uses as well as adjustments to how the model estimates tax collections and distributions.²⁸

Among other things, the Statewide Model captures the indirect and induced economic activity resulting from the direct project effects. This is accomplished by using large amounts of data specific to the Florida economy and fiscal structure. Mathematical equations²⁹ are used to account for the relationships (linkages and interactions) between the various economic agents, as well as likely responses by businesses and households to changes in the economy.³⁰ The model also has the ability to estimate the impact of economic changes on state revenue collections and state expenditures in order to maintain a balanced budget by fiscal year.

When using the Statewide Model to evaluate economic programs, the model is "shocked"³¹ using static analysis estimates of the initial or direct effects attributable to the projects funded by the incentives. In this analysis, direct effects are essentially the changes experienced by the businesses receiving the grants. The combined annual direct effects ("shocks") took the form of:

- Removal of the incentive payments from the state budget, with a corresponding award to businesses as subsidies to production.
- Incorporation of capital investments or residual capital benefits related to the project.
- Increased outputs based on retained and created jobs attributed to the project.

²⁶ Section 288.0001, F.S., as created by s. 1, ch. 2013-39, Laws of Florida & s. 1, ch. 2013-42, Laws of Florida.

²⁷ The statewide economic model was developed using GEMPACK software with the assistance of the Centre of Policy Studies (COPS) at Victoria University (Melbourne, Australia).

²⁸ Reports prior to January 1, 2017 have 2009 as the base year. Reports as of January 1, 2017 have 2011 as the base year.

²⁹ These equations represent the behavioral responses to economic stimuli – to changes in economic variables.

³⁰ The business reactions simulate the supply-side responses to the new activity (e.g., changes in investment and labor demand).

³¹ In economics, a shock typically refers to an unexpected or unpredictable event that affects the economy, either positive or negative. In this regard, a shock refers to some action that affects the current equilibrium or baseline path of the economy. It can be something that affects demand, such as a shift in the export demand equation; or, it could be something that affects the price of a commodity or factor of production, such as a change in tax rates. In the current analysis, a shock is introduced to remove the impact of the incentive on the economy.

After the direct effects are developed and estimated, the model is then used to estimate the additional—indirect and induced—economic effects generated by the projects, as well as the supply-side responses to the new activity, where the supply-side responses are changes in investment and labor demand arising from the new activity. Indirect effects are the changes in employment, income, and output by local supplier industries that provide goods and services to support the direct economic activity. Induced effects are the changes in spending by households whose income is affected by the direct and indirect activity.

All of these effects can be measured by changes (relative to the baseline) in the following outcomes:

- State government revenues and expenditures
- Jobs
- Personal income
- Florida Gross Domestic Product
- Gross output
- Household consumption
- Investment
- Population

EDR's calculation of the Return-on-Investment uses the model's estimate of net state revenues and expenditures. Other required measures for this report include the number of jobs created, the increase or decrease in personal income, and the impact on gross domestic product, all of which are included in the model results.

Key Assumptions

The following key assumptions are used in the Statewide Model to determine the economic benefits of the Microfinance Loan and Guarantee programs. Some of the assumptions are used to resolve ambiguities in the literature, while others conform to the protocols and procedures adopted for the Statewide Model.

1. The analysis assumes that the two programs were the determining factor in the ability of recipient businesses to achieve financing, since the program was created and designed to expand access to credit in the state.
2. The analysis assumes that the influence of any federal incentives awarded to state-funded projects is immaterial to the size and location of the project. This is also true for local incentives.
3. Unless otherwise specified, the analysis assumes all data provided by DEO related to projects was complete and accurate.
4. The analysis assumes businesses received the full value of the state incentives and that related costs due to federal taxes or consultant fees are immaterial to the decision making process.
5. The analysis assumes that given the time span under review, applying discount rates would not prove material to the outcome.

6. The analysis assumes that any expenditure made for incentives is a redirection from the general market basket of goods and services purchased by the state. Similarly, any revenue gains from increased business activities are fully spent by the state.
7. The analysis assumes the relevant geographic region is the whole state, not individual counties or regions. The Statewide Model does not recognize that any economic benefit arises from intrastate relocation. However, the model accounts and makes adjustments for the fact that industries within the state cannot supply all of the goods, services, capital, and labor needed to produce the state's output.
8. The analysis assumes that businesses treated the incentives as subsidies. The subsidies lowered the cost of production for each individual firm.
9. The analysis assumes distribution of capital purchases by each business was the same as the industry in which it operates. This assumption was made because data was not available regarding the specific capital purchases associated with each project. It is also assumed that the businesses within a program were not large enough to affect the rate of return on capital within the industries in which the businesses operated.
10. The analysis assumes that the output from included projects did not displace the market for goods and services of existing Florida businesses. To do this, output associated with the businesses was assumed to be exported to the rest of the world. The rest of the world is defined as other states or the international market. Excluded projects that were Florida market or resource dependent would have displaced other activity.
11. The analysis assumes that businesses are indifferent between tax credits and cash awards and will not change their behavior based on the type of incentive award given.
12. The analysis assumes all businesses receiving loans continue operations throughout the period of review.

Key Terms

In the pages that follow, the analysis for each program includes diagnostic tables describing the composition and statistics of the projects under review. Key terms used in the tables are described below:

State Payments in the period of review (window of review) \$(M) – Represents the amount of state payments made to the program in each fiscal year.

Total Net State Revenues \$(M) – Represents the amount of new state revenue generated by the program in each fiscal year.

Personal Income (Nominal \$(M)) – Reflects income received by persons from all sources. It includes income received from participation in production as well as from government and business transfer payments. It is the sum of compensation of employees (received), supplements to wages and salaries, proprietors' income with inventory valuation adjustment (IVA) and capital consumption adjustment (CCAdj), rental income of persons with CCAdj, personal income receipts on assets, and personal current transfer receipts, less contributions for government social insurance.

Real Disposable Personal Income (Fixed 2010-11 \$(M)) – Reflects total after-tax income received by persons; it is the income available to persons for spending or saving.

Real Gross Domestic Product (Fixed 2010-11 \$(M)) – Measures the state's output; it is the sum of value added from all industries in the state. GDP by state is the state counterpart to the Nation's gross domestic product.

Consumption by Households and Government (Fixed 2010-11 \$(M)) – Reflects the goods and services purchased by persons plus expenditures by governments consisting of compensation of general government employees, consumption of fixed capital (CFC), and intermediate purchases of goods and services less sales to other sectors and own-account production of structures and software. It excludes current transactions of government enterprises, interest paid or received by government, and subsidies.

Real Output (Fixed 2010-11 \$(M)) – Consists of sales, or receipts, and other operating income, plus commodity taxes and changes in inventories.

Total Employment (Jobs) – Provides estimates of the number of jobs, full time plus part time, by place of work. Full time and part time jobs are counted at equal weight. Employees, sole proprietors, and active partners are included, but unpaid family workers and volunteers are not included.

Population (Persons) – Reflects first of year estimates of people, including survivors from the previous year, births, special populations, and three types of migrants (economic, international, and retired).

Description of the Data

The DEO is the source of Microfinance Loan Program information, as provided by the respective program administrators. Two entities are under contract to administer the loan program: the Florida Black Business Support Corporation (FBBSC), which received \$300,000, and OUR MicroLending, LLC, which received \$4,825,000. Project job and wage information represents the loan applicant's projection at the time of application.

Through June 30, 2017, the Florida Black Business Support Corporation made 10 loans totaling \$274,964, one-half of which was state funds, to 7 businesses. Loan terms ranged from 4 to 12 months, at interest rates from 13.25 to 14 percent. The purpose of all loans was for working capital. The FBBSC reported 21 jobs created and 24 jobs retained. Wages ranged from \$19,220 to \$125,000, for an average of \$35,811.

Through June 30, 2017, OUR MicroLending made 166 loans totaling \$2,415,850, one-half of which was state funds, to 106 businesses. All of the loan terms were for 12 months, at an interest rate of 13.25 percent. DEO reports the purpose of these loans was for working capital. The OUR MicroLending reported 24 jobs created and 460 jobs retained.

The data show that over the 30 months (2½ years) of the loan program, 26.25 percent of the initial award to both loan administrators has been loaned to qualified borrowers. It is notable that lending by OUR Microlending increased sixty percent from FY 2015-16 to FY 2016-17 (from 55 to 88 loans).

The DEO is the source of Microfinance Guarantee Program information, as provided by EFI, the program administrator. As required by law, DEO contracts with EFI to administer the Guarantee program, which has received the allocated \$4,825,000.

For the two-year period from July 1, 2015 through June 30, 2017, EFI made 13 loan guarantees totaling \$1,683,278, one-half of which was backed with state funds. All loans were for a term of 36 months. The purpose of all loans was for business or real estate purchases (4), working capital (5), and equipment (4). EFI reports 104 jobs created, with wages averaging \$32,691, and 96 jobs retained by Guarantee recipients.

The data show that over the 24 months (2 years) of the guarantee program, 17.4 percent of the initial award to EFI has been used to guarantee loans to qualified borrowers.

Evaluation Considerations

The statutory purpose and design of a program are key considerations in its evaluation. The stated purpose of the Microfinance Loan and Guarantee programs is to increase access to credit for entrepreneurs and small businesses in Florida. These programs are not designed and administered like an economic development program. Program administrators do not screen projects for Florida market or resource dependency or evaluate projects for the ROI to the state as DEO does for state economic development incentives. While expanding “job opportunities for this state’s workforce” is an expressed intent of these programs, this is not a condition for receipt of a loan or loan guarantee.

EDR is charged with evaluating the Microfinance Loan and Guarantee programs in the same way it evaluates other state economic development programs. To enable this evaluation, DEO provided related state program expenditures and project information regarding the economic output generated by recipient businesses. This output is primarily from the creation or retention of jobs by assisted businesses.

From this information, EDR calculated the ROI to the state. All project information is reported in the aggregate.

As with previous evaluations, EDR’s calculation of ROI is based on the net economic impact rather than the gross economic activity generated by or attributed to program projects. The impact is due to new economic activity induced by a state subsidy after taking account of what would have occurred in the absence of this particular investment. EDR employs a number of approaches to isolate the new economic activity, including an assessment of the “but-for” assertion and culling “Market and Resource Dependent” projects.³² The resulting net economic benefit may then be proportionately attributed to all project contributors (in this case, lenders) or contributing public programs. Culling “Market and Resource Dependent” projects and proportionally attributing the economic benefit are strategies used to derive a credible estimate of the programs’ ROI.

³² Culling refers to removing the economic benefit of a particular project if it is determined to rely on Florida’s markets or resources and would have existed in Florida in the absence of the incentive. In circumstances where demand is increasing, the subsidy merely creates a competitive advantage for the recipient relative to non-recipients. In this case, the subsidy is unnecessary and potentially harmful to the efficient operation of the market. While the retention, expansion or relocation of market or resource dependent firms may have a localized economic impact, there is no net positive economic benefit to the state.

For further details, see EDR’s 2017 “Economic Evaluation for Select State Economic Development Incentive Programs,” Appendix ONE, pp. 37-46 @ <http://edr.state.fl.us/Content/returnoninvestment/ROISELECTPROGRAMS2017final.pdf>

ANALYSIS & FINDINGS

Program ROI

The data submitted to DEO from OUR Microlending, Inc. was deficient in two respects: incomplete NAICS codes for the businesses receiving loans and unverified wage data for the new and retained jobs. To remedy these deficiencies, EDR first replaced the erroneous NAICS codes with codes consistent with the business name and descriptions. Second, EDR used the average wage for the corresponding NAICS code in the calculation of output from loans for all of the businesses.

After incorporating these changes to the data, the reported economic activity from Florida market dependent businesses receiving loans (or guarantees) were excluded from calculation, and the resulting net economic benefit was apportioned between contributing lenders and the state's investment. As shown in Tables 1 and 2, EDR calculates the state's ROI for the Loan program to be 0.15 and 0.08 for the Guarantee program. Tables 1 and 2 also show the number of jobs created, the increase or decrease in personal income, and the impact on state gross domestic product from the direct, indirect, and induced effects of the state's investment.

Table 1. Economic Impact of the Microfinance Loan Program

		15-16	16-17	17-18	Total
State Payments in the Window	Nominal \$ (M)	5.2	0.0	0.0	5.2
Total Net State Revenues	Nominal \$ (M)	0.0	0.3	0.4	0.8
Return-on-Investment by Year		-	-	-	
Return-on-Investment for the 3 year period					0.15

		15-16	16-17	17-18	Total		Average per Year
Personal Income	Nominal \$ (M)	(0.4)	10.9	13.4	23.9		8.0
Real Disposable Personal Income	Fixed 2010-11 \$ (M)	(0.5)	8.2	10.1	17.8		5.9
Real Gross Domestic Product	Fixed 2010-11 \$ (M)	0.3	9.0	9.9	19.2		6.4
Consumption by Households and Government	Fixed 2010-11 \$ (M)	(0.3)	7.2	9.1	16.0		5.3
Real Output	Fixed 2010-11 \$ (M)	0.6	16.5	17.1	34.2		11.4

		15-16	16-17	17-18	Minimum	Maximum	Average per Year
Total Employment	Jobs	20	70	55	20	70	48
Population	Persons	0	0	32	0	32	11

Table 2. Economic Impact of the Microfinance Guarantee Program

		15-16	16-17	17-18	Total
State Payments in the Window	Nominal \$ (M)	4.8	0.0	0.0	4.8
Total Net State Revenues	Nominal \$ (M)	0.3	0.0	0.1	0.4
Return-on-Investment by Year		0.1	-	-	
Return-on-Investment for the 3 year period					0.08

		15-16	16-17	17-18	Total		Average per Year
Personal Income	Nominal \$ (M)	8.8	1.5	1.5	11.8		3.9
Real Disposable Personal Income	Fixed 2010-11 \$ (M)	6.7	0.9	0.8	8.4		2.8
Real Gross Domestic Product	Fixed 2010-11 \$ (M)	7.6	0.5	0.6	8.6		2.9
Consumption by Households and Government	Fixed 2010-11 \$ (M)	6.0	0.8	0.8	7.6		2.5
Real Output	Fixed 2010-11 \$ (M)	15.4	1.7	1.6	18.7		6.2

		15-16	16-17	17-18	Minimum	Maximum	Average per Year
Total Employment	Jobs	64	(6)	(3)	(6)	64	18
Population	Persons	0	32	32	0	32	21

Types of Businesses

Tables 3 and 4 show the industry composition of businesses receiving loans and guarantees through the two programs, as categorized by the North American Industry Classification System (NAICS) codes. Of the 176 loans through the Loan program, forty-nine were made to businesses in the Transportation and Warehousing industry, with most loans made to trucking companies, couriers and delivery services. Twenty-nine loans were made to industries in the “Other Services” category, most of which were beauty salons/barber shops and auto-detailing businesses. Twenty-seven loans were to businesses in Retail Trade, and 19 in Construction. Eleven loans were to “Accommodation and Food Service” businesses, and 10 were to businesses categorized under Wholesale Trade. Four loans were made to Manufacturing businesses.

Of the thirteen loan guarantees through the Guarantee program, 3 were to businesses in the “Other Services” category and 3 were to “Accommodation and Food Service” businesses. Two loan guarantees were made to Construction businesses, and 2 were to Manufacturing enterprises.

To produce the ROIs shown above and on the previous page, 156 of the 176 loans were culled from the Loan program, and 11 of the 13 loans were culled from the Guarantee program.

Table 3. Industry Composition for Loan Program

NAICS	2012 NAICS Description	Number of Loans	Total Amount of Loans	DEO Portion of Loans	Jobs Created	Jobs Retained	Total Jobs
23	Construction	19	\$ 321,714	\$ 160,857	19.5	50.5	70
31-33	Manufacturing	4	\$ 90,000	\$ 45,000	3	20	23
42	Wholesale Trade	10	\$ 211,000	\$ 105,500	3	37	40
44-45	Retail Trade	27	\$ 340,000	\$ 170,000	1.5	37.5	39
48-49	Transportation and Warehousing	49	\$ 812,500	\$ 406,250	3	98	101
51	Information	1	\$ 9,000	\$ 4,500	0	2	2
52	Finance and Insurance	2	\$ 100,000	\$ 50,000	0	2	2
53	Real Estate and Rental and Leasing	3	\$ 48,000	\$ 24,000	0	24	24
54	Professional, Scientific, and Technical Services	7	\$ 88,200	\$ 44,100	0	17	17
56	Administrative and Support and Remediation Services	6	\$ 111,000	\$ 55,500	1	57	58
61	Educational Services	1	\$ 7,000	\$ 3,500	0	1	1
62	Health Care and Social Assistance	6	\$ 58,000	\$ 29,000	0	11	11
71	Arts, Entertainment, and Recreation	1	\$ 18,000	\$ 9,000	0	3	3
72	Accommodation and Food Services	11	\$ 181,000	\$ 90,500	3	59	62
81	Other Services (except Public Administration)	29	\$ 295,400	\$ 147,700	10.5	65	75.5
Loan Total		176	\$ 2,690,814	\$ 1,345,407	44.5	484	528.5

Table 4. Industry Composition for Guarantee Program

NAICS	2012 NAICS Description	Number of Loans	Total Amount of Loans	DEO Portion of Loans	Jobs Created	Jobs Retained	Total Jobs
23	Construction	2	\$ 382,979	\$ 191,489	22	24	46
31-33	Manufacturing	1	\$ 100,000	\$ 50,000	18	7	25
44	Retail Trade	1	\$ 50,000	\$ 25,000	15	0	15
61	Educational Services	1	\$ 80,000	\$ 40,000	17	0	17
62	Health Care and Social Assistance	1	\$ 105,200	\$ 52,600	1	1	2
72	Accommodation and Food Services	3	\$ 435,000	\$ 217,500	32	43	75
81	Other Services (except Public Administration)	3	\$ 530,100	\$ 265,050	9	26	35
Guarantee Total		13	\$ 1,683,279	\$ 841,639	114	101	215

Program Efficiency

In addition to addressing the ROI of these programs, EDR is required to “identify inefficiencies in the Microfinance Loan Program and Microfinance Guarantee Program and provide recommendations for changes to the programs.”³³ Other than issues with the initial implementation, a review of these programs show they are an efficient means to meet program goals: to make available “...short-term, fixed-rate microloans in conjunction with business management training, business development training, and technical assistance to entrepreneurs and newly established or growing small businesses...”³⁴ First, these programs “avoid duplicating existing programs” by targeting small loans which arguably fills a gap in pre-existing state-funded programs. Second, almost all of the initial (and to date, only) state appropriation for these programs is preserved, as deductions for administrative expenses are statutorily capped or prohibited. Further, program funds are required to be reinvested and maintained as a recurring source of program funding. Finally, contracting with third-party service providers precludes the necessity to replicate systems and processes within the DEO. These program design features will contribute to the efficient operation and continued cost-efficiency of the Microfinance programs.

³³ Section 288.9937, F.S. For EDR’s purposes, efficiency is defined as acting or producing effectively with a minimum of waste, delay, expense, or unnecessary effort. Cost-efficient is defined as cost-effective, productive or effective in relation to its cost.

³⁴ Section 288.9934(1), F.S.

1. Targeting small loans arguably fills a gap in pre-existing state-funded programs.

The Florida Microfinance Act created the Microfinance Loan and Microfinance Guarantee programs to increase access to credit for entrepreneurs and small businesses in Florida. These programs are similar to the federally-funded State Small Business Credit Initiative (SSBCI) programs administered by DEO and EFI, except that the SSBCI programs have “a stated minimum loan size of \$250,000 and as such, tend to complement rather than compete with the Microfinance Programs.”³⁵

2. DEO’s administrative expenses are minimal, and support the cost-efficiency of the Microfinance programs.

DEO has designated 1.25 FTE to manage the Microfinance programs.³⁶ DEO also budgets resources to market the programs.³⁷ While DEO is authorized to assess a nominal annual fee against Microfinance Loan administrators, DEO staff report they do not levy this fee.³⁸ There is no authority to assess a similar fee against the Guarantee program.

3. Allowable deductions from the state awards by program administrators are minimal for the Loan program and prohibited for the Guarantee program. Further, repaid loans and residual loan guarantees are recycled into the program,³⁹ which advances the cost-efficiency of the programs.

Loan program administrator service fees are limited to one percent of the total award from DEO.⁴⁰ Administrators also retain the interest on the loans, which is capped at the current prime rate plus 1000 basis points.⁴¹ The costs for training for and technical assistance to borrowers provided in conjunction with the microloans are not paid with program funds.⁴² Further, upon expiration or termination of the contract with loan administrators, all repaid loan principal and interest earned on escrowed funds must be remitted to DEO, so nearly all of the initial appropriation is recovered.⁴³ For the Guarantee program, EFI is restricted from using DEO awards (and any interest earned on escrowed funds) to offset associated administrative costs,⁴⁴ and loan guarantees that are no longer needed are reused for additional loan guarantees. Because the Microfinance programs supplement existing programs, it is not

³⁵ Microfinance Programs Annual Report, 2017. Division of Community Development, Florida Department of Economic Opportunity, November 1, 2017, p. 3. <http://www.floridajobs.org/docs/default-source/reports-and-legislation/microfinancenannualreportfy16-17.pdf?sfvrsn=2>

³⁶ DEO report their costs for FY 2016/17: \$92,862.

³⁷ DEO reports their total marketing costs to date: \$56,317.

³⁸ Section 288.9934(5), F.S., authorizes DEO to assess “an annual fee or interest of up to 80 percent of the Federal Funds Rate as of the date specified in the contract for state funds received under the loan program.”

³⁹ At least for the term of the initial contract with the loan administrator, loan funds are recycled into the program. While s. 288.9934(3)(a), F.S., infers the loan program “be maintained as a long-term and stable source of funding for the program,” paragraph (3)(a) does not specifically authorize a subsequent round of awards to program administrators at the end of the initial three-year contracts.

⁴⁰ Section 288.9934(5)(b), F.S. Loan administrators are also authorized to assess an application fee, late fees, and costs and fees incurred for any collection efforts necessitated by a borrower’s default. See s. 288.9934(9), F.S.

⁴¹ Section 288.9934(9)(d)6., F.S. On May 31, 2017, the capped interest rate was 14 percent. This restriction is not imposed on loans associated with the Guarantee program, as the rates are set by the lenders.

⁴² Training costs are covered by the training provider, the FSBCD Network.

⁴³ Section 288.9934(6)(a), F.S.

⁴⁴ Section 288.9935(6), F.S., and pursuant to the contract with DEO.

necessary to create a parallel administrative infrastructure – with associated administrative costs – to enable lending.

4. Contracting with existing service delivery systems to provide direct loan services is more efficient and cost-efficient than replicating these respective systems within DEO.

For the Microfinance Loan program, the governing statutes require DEO to contract with at least one but not more than three loan administrators.⁴⁵ The statutes require DEO to contract with Enterprise Florida, Inc., to administer the Microfinance Guarantee program.⁴⁶ Outsourcing direct service delivery allowed DEO to circumvent recruiting and training program staff in the target markets, and also avoid developing processes for recruiting borrowers, evaluating loan applications, underwriting and servicing loans, and coordinating training and technical assistance. Outsourcing also capitalized on existing relationships between the Guarantee program administrator and partners in the local lending community. All of these factors contribute to timely and efficient operation of the programs.

The cost-efficiency of the Microfinance programs is especially evident relative to other DEO-administered loan or investment programs. For example, Black Business Investment Corporations (BBICs) may use nine percent of a Black Business Loan Program grant to cover technical support to business enterprises, and up to twelve percent of the grant to cover direct administrative costs.⁴⁷

The Florida New Markets Development Program (NMDP), a subsidy designed to “encourage capital investment in rural and urban low-income communities,”⁴⁸ imposes no restrictions on the amount of program funds retained to cover administrative expenses. Briefly, the NMDP allows taxpayers (investors) to earn tax credits by investing in qualified Community Development Entities (CDEs, or intermediaries) that make certain Qualified Low-Income Community Investments (QLICIs) in Qualified Active Low-Income Community Businesses (QALICBs). The equity from the sale of tax credits to investors is typically combined with loans from commercial lenders. The complex inter-related, multiple-step transaction structures used by CDEs generate significant transaction costs. These costs are recovered through deductions from project loans; and through transaction, origination and closing fees, and recurring asset management fees assessed against the recipient QALICB. In lieu of levying fees, CDEs may retain the principal from the investor’s (taxpayer’s) portion of the loan to or equity investment in the QALICB at the end of the loan term. CDEs may also assess additional fees against the QALICB for third-party reviews of the transaction. Total administrative costs (and related CDE retentions) can exceed the amount of equity generated by the sale of tax credits provided by the state.⁴⁹

⁴⁵ Section 288.9934(3)(a), F.S.

⁴⁶ Section 288.9935(3), F.S.

⁴⁷ Section 288.7102(7)(c), F.S.

BBICs are not-for-profit subsidiaries of financial institutions or consortia of financial institutions investing in or lending to small businesses. BBICs provide loans, loan guarantees, and technical assistance to business enterprises. Currently, two BBICs participate in the program. *Also see OPPAGA, “Agency Review – Enterprise Florida, Inc., and Department of Economic Opportunity, Report No. 16-09 p. 29* <http://www.oppaga.state.fl.us/MonitorDocs/Reports/pdf/1609rpt.pdf>

For an early history of BBIC participation in state funded loan grant programs, see

http://archive.flsenate.gov/data/Publications/2006/Senate/reports/interim_reports/pdf/2006-105cmlong.pdf

⁴⁸ Section 288.9912, F.S.

⁴⁹ For an evaluation of the Florida NMDP, see The Office of Economic and Demographic Research, *“Economic Evaluation for Select State Economic Development Incentive Programs,”* January 2017, pp. 32-36, and 47-72.

Issues Regarding Effectiveness

EDR's review of the Microfinance programs is limited to evaluation of the economic benefits (ROI) and efficiency (or cost-efficiency) of the programs – specifically DEO's administration of the program and the program design.⁵⁰ Others have addressed program effectiveness and offer observations that inform EDR's understanding of the program. Their measures of "effectiveness and value"⁵¹ include program participation – from both program administrators and borrowers – geographic reach, and program features that may affect program Return-on-Investment to the state.

In 2016, the Office of Program Policy Analysis and Government Accountability (OPPAGA) published an Agency Review of EFI and DEO. The report addressed a wide range of issues, to include the effectiveness of the Microfinancing Loan program, noting that:

According to program administrators and DEO staff, Microfinance Loan program participation is limited by short loan repayment terms. The program has a one-year repayment period for participating businesses, which results in large monthly payments that many small businesses are unable to repay. Furthermore, program administrators reported that the administrative fee (1.0%) is not sufficient to cover state program costs. Consequently, contractors use revenue from other non-state programs to subsidize state program costs.⁵²

The OPPAGA report also finds that:

The lack of geographic reach also limits program participation. There are currently only two MLP administrators, located in Miami and Tallahassee. Although technically meant to serve the entire state, the statutory requirement that loan administrators meet one-on-one with businesses essentially limits their service area and the number of businesses they are able to serve. For example, the MLP administrator located in Miami only services loans in four counties.⁵³

DEO has implied underuse of both the Loan and Guarantee programs in its 2016 Annual Report:

The Microfinance Loan Program has shown success during its first full year, but changes may be needed in the future to further the utilization of both programs...DEO recommends working with loan administrators and stakeholders of both programs to better define any challenges that may currently exist with the programs. Working collaboratively, all stakeholders can develop ways to enhance the program to ensure that it accomplishes the goal of stimulating access to credit for entrepreneurs and small businesses.⁵⁴

While there has been a notable increase in activity through the Loan program in the past fiscal year, participation in both programs is short of their potential, as evidenced by unused program funds.

⁵⁰ It does not include an evaluation of the three contract administrator's processes for recruiting and evaluating borrowers, monitoring compliance, recovering delinquent loans, etc.

⁵¹ This is the requirement in OPPAGA's evaluation of state economic development programs subject to triennial reviews in s. 288.001, F.S.

⁵² "Agency Review – Enterprise Florida, Inc., and Department of Economic Opportunity," Report No. 16-09. <http://www.oppaga.state.fl.us/MonitorDocs/Reports/pdf/1609rpt.pdf>, p. 29.

⁵³ *Ibid.*, p. 29.

⁵⁴ "Microfinance Programs Annual Report," Division of Community Development, DEO of Economic Opportunity, November 1, 2017. P. 11. <http://www.floridajobs.org/docs/default-source/reports-and-legislation/microfinanceannualreportfy16-17.pdf?sfvrsn=2>

These observations are echoed, in part, by the DEO commissioned 2014 report from The Center for Economic Forecasting and Analysis, of the Florida State University.⁵⁵ The report suggested that “the administrative fee should be established by the loan administrators in order to cover the cost of program development, delivery and reporting.” In addition, the cap on closing fees should be lifted in order to ultimately facilitate increasing the number of borrowers served over time. The report also suggested the longer loan terms may be warranted if loans were tailored to “focus on productive capital, or assets used in more than one production cycle...”⁵⁶

The recommendations regarding investments in productive capital are supported by EDR’s observations regarding ROI for state economic development incentives.⁵⁷ While removing or increasing the interest rate cap and limits on administrative fees may expand program participation – directly with lenders and potentially with borrowers – it will likely diminish the cost-effectiveness of the loan program. Conversely, to the extent current program parameters contribute to its underuse, appropriated state funds are not invested in the economy.

Conclusion

A review of the Microfinance Loan Program and Microfinance Guarantee Program shows they are an efficient means to meet program goals. The programs supplement or complement existing programs, providing capital to enable them to expand services (loans and loan guarantees) to qualified borrowers in the target market.

However, it may be that the efficient design of the Loan program diminishes its effectiveness, as demonstrated by the lack of demand for capital from eligible program administrators. The training requirement, interest rate cap and limits on administrative fees and other administrative requirements may deter lenders from participating, notwithstanding the access to very inexpensive capital from the program.

As for both the loan and guarantee program, it is possible that the low rate participation of qualified borrowers is due to weakened demand, as the economy is recovering and traditional (and non-traditional) lending institutions may be meeting the needs of the market. It is also possible that program use will grow as the program matures, as evidenced by the increased rate of lending by OUR Microlending in the third year of the loan program.

⁵⁵ Section 288.9934(11), F.S., required DEO to commence or commission a study to “...identify methods and best practices that will increase access to credit to entrepreneurs and small businesses in this state. The study must also explore the ability of, and limitations on, Florida nonprofit organizations and private financial institutions to expand access to credit to entrepreneurs and small businesses in this state.”

See Julie Harrington and Martijn Niekus. 2014. “An Economic Analysis Study to Identify the Methods and Best Practices to Increase Access to Credit to Entrepreneurs and Small Businesses in Florida, Center for Economic Forecasting and Analysis, the Florida State University. December 31, 2014, p. 30-31.

http://www.floridajobs.org/community/MLB_MicrofinanceStudyReport.pdf

⁵⁶ This would include equipment, machines, tools and other, used in the process of providing goods and services for more than once production cycle or a year.

⁵⁷ “Return on Investment in Florida Practice,” February 4, 2015. p.8.

http://edr.state.fl.us/Content/returnoninvestment/ROI_InFloridaPractice.pdf

Recommendations

If the Legislature intends the Microfinance Loan program to operate beyond 2017, it should clarify that the principal from repaid loans recovered by DEO at the termination of its contract with the loan administrators be reallocated to the current or newly-qualified loan administrators.

The Legislature should also consider focusing the programs on entrepreneurship by targeting only businesses with innovations that satisfy a specific need or result in revolutionary products. The program criteria would otherwise remain the same. This recommendation is based on information contained in Appendices One and Two, as well as an attempt to cure some of the market dependency.

Perhaps with a more limited focus, DEO would have better success in marketing the program.

Appendix One: AN OVERVIEW OF MICROFINANCING IN THE U.S. AND THE DEVELOPING WORLD

Introduction

In 2014, the Florida Legislature created the Microfinance Loan and Microfinance Guarantee programs through the Florida Department of Economic Opportunity (DEO) to increase access to credit for entrepreneurs and small businesses.⁵⁸ Florida's program may be one expression of a greater international microfinance movement which "seeks to expand economic opportunities for individuals and to foster community economic development by providing small loans and other business services to people who have been traditionally underserved by mainstream financial institutions."⁵⁹

This overview will briefly define microfinancing, and discuss its evolution in the international context and adaptation in the U.S.

What is Microfinancing?

Microcredit is generally described as lending very small amounts of funds to a person or project who would otherwise be unable to obtain a loan. Sherratt (2016, 3) adds these loans are "typically at higher interest rates than a traditional bank charges, but below those of a money lender." While the terms microcredit and microfinance are often used interchangeably, they are distinct. Microcredit is the provision of a loan, and microfinance is the provision of a range of financial services, which may include microcredit, savings, insurance, and payments and remittances.⁶⁰

Microfinancing in the U.S. is considered a subset of small business lending, typically differentiated by the limit of the loan amount – \$50,000 – and the size threshold of eligible businesses – five or fewer employees.⁶¹ Microfinancing is targeted to those unqualified for loans from commercial banks, and are designed to advance them into the mainstream lending community. Schreiner and Morduch (2001, 42) note that "the 'unbanked' lack access to more than just loans. In the United States, the recognition has meant adding training programs."

Internationally, microfinancing is provided through Microfinance Institutions (MFIs). In the U.S., MFIs are also identified as Microfinance Development Organizations (MDOs), as they provide some combination of loans, technical assistance, training and other services to microenterprises. Estimates as to the number of MDOs in the U.S. vary. The Microenterprise Fund for Innovation, Effectiveness, Learning and Dissemination (FIELD) at the Aspen Institute reports there are 677 MDOs that have reported data to their microTracker since 2008. Of these 677 MDOs, 185 are financing/credit-led organizations.⁶²

⁵⁸ Sections 49 - 57, ch. 2014-218, L.O.F.

⁵⁹ Ben Bernanke, Remarks at the ACCIÓN Texas Summit on Microfinance in the United States, San Antonio, Texas November 6, 2007. <https://www.federalreserve.gov/newsevents/speech/bernanke20071106a.htm>

⁶⁰ Sengupta and Aubuchon (2008, 10); Schreiner and Morduch (2001); and <https://www.microfinancegateway.org/what-is-microfinance>

⁶¹ Until recently, loans of \$35,000 or less were considered microloans. However, the Small Business Administration now considers loans of \$50,000 to be microloans under their microloan program. <https://www.sba.gov/loans-grants/see-what-sba-offers/sba-loan-programs/microloan-program>

⁶² FIELD staff note that there may be other MDOs that have not reported data to microTracker, and FIELD staff have not verified that all MDOs reporting continue in operation. FIELD's mission is "to identify, develop and disseminate best practices, and to educate funders, policymakers and others about microenterprise as an anti-poverty strategy." <http://fieldus.org>

MFIs may be subsidized, mission-centered non-profit lenders; a mission-centered non-profit advancing to self-sufficiency by adopting a financial systems approach to lending; or for-profit entities primarily responding to market forces, with less emphasis on a social mission.⁶³

Issues in International Microfinancing

The launch of the modern microfinance movement in the 1980s is credited to Muhammad Yunus, the 2006 Nobel Peace Prize winner and founder of Grameen Bank in Bangladesh. His Nobel Prize biography page states that “(h)is objective was to help poor people escape from poverty by providing loans on terms suitable to them and by teaching them a few sound financial principles so they could help themselves.”⁶⁴ The movement rapidly spread to other developing states. Bateman and Chang (2010, 2) assert that:

“...(b)y the 1990s, microfinance was the international development community’s highest-profile and most generously funded poverty reduction policy. The expectation began to form that an historically unparalleled poverty reduction and ‘bottom-up’ economic and social development episode was in the making.”

Over the decades MFIs have evolved, largely adopting a financial systems model with an emphasis on institutional self-sufficiency. Microfinancing became commercialized as banks and mainstream finance invested in the expanding marketplace and non-governmental organizations “transformed to become non-bank financial institutions or microfinance banks.”⁶⁵ Brau and Woller (2004, 2) offer this appraisal of the appeal of microfinancing:

“The rise of the microfinance industry represents a remarkable accomplishment taken within historical context. It has overturned established ideas of the poor as consumers of financial services, shattered stereotypes of the poor as not bankable, spawned a variety of lending methodologies demonstrating that it is possible to provide cost-effective financial services to the poor, and mobilized millions of dollars of “social investment” for the poor... microfinance offered the potential to alleviate poverty while paying for itself and perhaps even turning a profit—doing well by doing good. This potential, perhaps more than anything, accounts for the emergence of microfinance onto the global stage.”

This “third way”⁶⁶ to address global poverty has an estimated reach of two hundred million borrowers.⁶⁷

The promise of the microfinance movement was challenged by program crises in India (2006 & 2010), Morocco (2007), Bangladesh (2007), Pakistan (2008), Bosnia (2008), Nicaragua (2009) and Nigeria (2010).⁶⁸ The challenge also came from increased scrutiny of program effectiveness. Mendelson and

⁶³ See Gomez and Edgcomb (2011) for a comparison of non-profit and for-profit MFIs in the U.S. Also see Lieberman et al (2012, 59-66); Chandra and Arun (2011, 2); and Servon (2006, 354).

⁶⁴ https://www.nobelprize.org/nobel_prizes/peace/lauriates/2006/yunus-bio.html For a pre-1980s history of microcredit, see Roodman (2012a, 36-64).

⁶⁵ Lieberman et al (2012, 19). Also see Sherratt (2016, 5-20); Sinclair (2012, 114-115); Roodman (2012a, 232-247); and Chandra and Arun (2011, 6-10).

⁶⁶ “Third way” is a general description of a ‘centrist’ approach to policy development, which attempts to reconcile liberal and conservative perspectives. In this context, see Schreiner and Morduch (2001, 3); and Bateman and Chang (2011, 22).

⁶⁷ Sherratt (2016, xiii); Adler and Waldschmidt (2013, 124); and Banerjee (2013, 488).

⁶⁸ The “typology of problems or risks” identified in these crises include “poor governance practices, fraud, methodological flaws, uncontrolled growth of the MFI, mission drift, uncontrolled growth in select markets leading to over-lending and over-

Rozas (2014, 5) report that while early studies showed “substantial improvement in borrowers’ livelihoods,” subsequent research called these assessments into question:

“The tremors set off by all this research came not just from the findings but also from the timing. To learn that microfinance was bad at helping the poor was one thing. To learn it just as microfinance seemed to be collapsing in one of its biggest markets was another.”

In 2011, a systematic review of microfinance evaluations to date (Duvendack *et al*, 2011, 2 and 75) found that “(d)espite the apparent success and popularity of microfinance, no clear evidence yet exists that microfinance programmes have positive impacts.”⁶⁹ Subsequent randomized control trials support this assessment.⁷⁰ In Roodman’s (2012b, 4) search for “what works” in microfinancing, he offers this perspective:

“On current evidence, the best estimate of the average impact of microcredit on the poverty of clients is zero. So microcredit as a whole appears neither to live up to the hype nor deserve the harshest attacks against it as enslavement by debt. It isn’t a miracle cure for poverty, and it is not the financial equivalent of cigarettes. Instead, the commonsense idea that credit can help in moderation and harm in excess appears close to the truth.”

Researchers, analysts, and practitioners suggested a number of reasons that microfinance (specifically, microcredit) fails to alleviate borrowers’ poverty:⁷¹

- Borrowers do not use the money for a productive use – loans were spent on general consumption, consumer goods, or to repay other loans;
- Lack of demand for borrower’s products or services, as borrowers produced or provided what was sufficiently available in the marketplace; and
- Effective interest rates were high, so business profits were insufficient to repay loans, to accumulate business capital, and increase personal wealth.

Bateman (2010, 64-111, 125; 2017, 127-143) addresses an unintended consequence of the microfinance movement, arguing that while some borrowers benefit from loans, the microfinance model largely impedes national development. He reasons, in part, that the microfinance model:

- Ignores the crucial role of scale economies -- microenterprises are unlikely to operate at minimum efficient scale, and thus are unlikely to survive in a competitive environment;
- As a supply-side initiative, it creates hyper-competition, which precipitates downward pressure on prices, income, wages and profits – disappointing new entrepreneurs and displacing existing producers;

borrowing, macroeconomic shocks, and state intervention.” Lieberman *et al* (2012, 30). *Also see* Bateman and Maclean (2017); Sinclair (2012); and Roodman (2012a, 252-259 and 270).

⁶⁹ The study screened 2,643 articles, from which 58 studies were examined in detail. The authors concluded that “it remains unclear under what circumstances, and for whom, microfinance has been and could be of real, rather than imagined, benefit to poor people.” *Also see* Terberger (2013, 188-192).

See Roodman (2012a, 148-174) and Bateman (2010, 61-77) for a critique of microfinance impact assessments.

⁷⁰ Sherratt (2016, 24, 28-34) and Banerjee (2013, 508).

⁷¹ Sherratt (2016, 29-30); Berlage and Jasrotia (2015); Hulme & Maitrot (2014); Saeed (2014); Banerjee (2013, 510-512); Sinclair (2012, 5-7, 65-66, 73, 78, 81-82, 200); Roodman (2012a, 200-201); Bateman and Chang (2011); Bateman (2010, 29-63, 118-122, 132-141); McFarquhar (2010); and Beck and Ogden (2007).

See Lieberman *et al* (2012, 30-31) for their assessment of program successes.

- Helps to deindustrialize and infantilize the local economy, as it misdirects scarce resources from small and medium-sized enterprises (SMEs) and new, creative, technically innovative ideas and institutions into very simple trading, retail and service operations; and
- Distorts and misdirects institutional responses to poverty.

Mendelson and Rozas (2014, 16-17) acknowledge these assessments, but respond that the demand for what microfinance offers “– the chance for poor people to get on the financial ladder – remains huge.” Further:

“We recognize the size of the challenges. But there is innovation everywhere, and the lessons from the hubristic early decades of microfinance have probably been learned. What’s left now that the smoke has cleared is an industry focused on how to roll out quality, demand-led financial services to the underserved from larger, commercial providers; Doing No Harm of course, but less myopically driven to Do Good.”

Roodman (2012a, 6 and 270) concludes that the strength of microfinancing “lies not in lifting people out of poverty – industrialization and jobs do that better...It lies, rather, in leveraging modest subsidies to build financial institutions and industries that give millions of poor families more control over their finances.”

The Centre for the Study of Financial Innovation (CFSI) periodically surveys financial institutions around the world to assess the risk they perceive in the microfinance industry. The preface to the 2014 report includes the following perspective:

“It may be that microfinance is at or close to an inflection point. What was, a decade ago, little more than a laboratory-scale experiment in bottom-up development has gone mainstream – and with that transition have come mainstream problems, notably client over-indebtedness. No doubt, these problems can be (and are being) tackled, but the important thing to realize is that they signify success, not failure. Microfinance is becoming normal.”⁷²

In summary, the microfinance movement has evolved from mission-oriented, community-based microcredit for the very-poor (an alternative to predatory moneylenders in the informal economy), to sustainable, commercial “financial inclusion,” which is branded as access to a full suite of financial services – including credit, savings, insurance, and payments – provided with quality to everyone who can use financial services with financial capability, through a diverse and competitive marketplace.⁷³

⁷² Lascelles, et al (2014). This survey was conducted in early 2014 and is based on 306 responses from 70 countries. The greatest number of responses were from the US (61), India (26), UK (24), and Mexico (15). Respondents include experts on microfinance, including practitioners, analysts, regulators and investors. North American response consisted mostly of investors, donors, networks and consultants serving MFIs in other parts of the world. The 2014 Report is the fifth in the series, dating back to 2008.

Some have argued that in this commercialization of microfinance, the movement has “lost its moral compass.” See Sherrott (2016, xiv-xv); Hulme and Maitrot (2014); and Sinclair (2012, 69-82, 211-216). For a specific example (the “Compartamos episode”), see Bateman (2010, 146-155). For an alternative perspective, see Schmidt (2013, 41-67).

⁷³ <http://www.centerforfinancialinclusion.org/about/who-we-are/our-definition-of-financial-inclusion>
Also, <https://www.un.org/development/desa/socialperspectiveondevelopment/issues/financial-inclusion.html> ;
Also see The Global Financial Development Report, 2014: Financial Inclusion. Published by the International Bank for Reconstruction and Development / The World Bank
http://siteresources.worldbank.org/EXTGLOBALFINREPORT/Resources/8816096-1361888425203/9062080-1364927957721/GFDR-2014_Complete_Report.pdf ; and <https://www.microfinancegateway.org/what-is-microfinance>

Assessing the Demand for Microfinancing in the U.S.

Lieberman *et al* (2012, 9) suggest that microfinancing is well suited to low-income developing countries due to the density of poverty and the lack of access to the formal banking sector. Does the relative scarcity of MFIs in the U.S. suggest a lack of demand for microfinancing? Hoy *et al* (2012, 4) note that assessing the demand for MFI services in the U.S. is a challenge:

“Although FIELD estimates a potential market of 10 million entrepreneurs, it is not certain that all of these individuals need microcredit. Unlike developing countries, the United States has a large and mature financial sector, which offers a broad range of credit options to potential borrowers, even if some of those options are relatively high cost. For example, some borrowers might prefer the convenience and immediacy of credit cards or payday loans to microloans, which often require training or financial education or have other transaction costs.”

Recent surveys by state and national small business organizations indicate that access to credit by their membership is now not a primary concern. The Florida Chamber of Commerce reported that “Economic Uncertainty” and “Access to Capital” were tied for fourth place in their April, 2017 survey for the Florida Small Business Index, with 10 percent each. When asked if they were able to obtain financing during the last 6 months, 39% replied yes, 11% replied no, and 50% responded they did not need capital financing.⁷⁴ In their 2016 Year-End Economic Report, the National Small Business Association reported that “small-business access to capital remains stubbornly unchanged with just 69 percent of small firms able to get adequate financing.”⁷⁵ The National Federation of Independent Businesses May, 2017 survey of their membership reported the following:

Thirty-one percent reported all credit needs met (down 1 point), and 51 percent explicitly said they did not want a loan. Only 1 percent reported that financing was their top business problem compared to 22 percent citing taxes, 19 percent citing the availability of qualified labor, and 13 percent regulations and red tape. Twenty-eight percent of all owners reported borrowing on a regular basis (down 3 points).⁷⁶

Relative to other business needs, it appears that obtaining financing ranks lower than the other concerns of survey respondents.

In contrast, the network of Federal Reserve Banks’ 2016 Small Business Credit Survey of employer firms reports that “(h)eading into 2017, small businesses expressed continued optimism while also reporting trouble making ends meet and accessing credit.” Among other things, their survey finds “persistent credit gaps for smaller-revenue firms (annual revenues of \$1M or less), stemming in part from weak credit scores and insufficient credit histories.”⁷⁷ Of 1,576 responses to their 2015 Small Business Credit

Lascelles, *et al* (2016) further qualified the change as “financial exclusion and inclusion – bringing basic (appropriate, affordable) financial services to the underserved in developing countries around the world, sometimes on a commercial basis but often with some form of subsidy, subvention or pump-priming by agencies either in-country or in the more developed economies of the world.” *Also see* Bateman (2017, 28-29).

⁷⁴ Pages 3 and 11. These results are based on 128 responses from “...a nonscientific, random sampling of small business owners in Florida...” http://www.flchamber.com/wp-content/uploads/2017/04/SBIS-Q2201720April_Final.pdf

⁷⁵ Pages 2 and 9. “Lack of available capital” ranked seventh of 15 options, with 51 percent of respondents stating that “economic uncertainty” posed significant challenges to the future growth and survival of their business.” (p. 5)

<http://www.nsba.biz/wp-content/uploads/2017/02/Year-End-Economic-Report-2016.pdf>

⁷⁶ (p. 2) <http://www.nfib.com/assets/SBET-May-2017.pdf>

⁷⁷ Executive Summary, p. iii <https://www.newyorkfed.org/medialibrary/media/smallbusiness/2016/SBCS-Report-EmployerFirms-2016.pdf>

Survey of non-employer firms, thirty-two percent reported they had applied for loans, and 41% of those “applicants were not approved for the funding they sought. A low credit score and insufficient collateral were the top reasons firms were not approved for credit.”⁷⁸

The surveys indicate there is a segment of the small-business sector unable to access conventional loans from formal financial institutions, deemed ‘unqualified’ for conventional loans due to their poor credit score, inadequate collateral, relative lack of business experience or insufficient history with mainstream banking.⁷⁹ It is the mission of MFIs in the U.S. to remedy these conditions by addressing borrowers’ deficiencies as well as providing affordable microfinancing, thereby facilitating their advancement into the mainstream financial community.

Microfinance in the US

As previously noted, the conditions that make microfinancing well suited to developing countries – the density of poverty and lack of access to the formal banking – do not exist to the same extent in the U.S. There are additional factors that may preclude the expansion of microfinancing in the U.S.:⁸⁰

- The availability of wage employment, for less hours, more pay and less risk than operating your own business – the highly skilled and better motivated individuals have alternatives to self-employment;
- A functional public safety net in the U.S. may be a disincentive to starting a business as it is an alternative to self-employment;
- Small businesses face strong competition from large retailers, restaurant chains, service providers, large manufacturers, imports, and agribusiness;
- As previously noted, availability of alternative credit sources, to include credit cards from commercial lenders, payday lenders, personal finance companies, check-cashing outlets, pawn shops, and increasingly Peer-to-Peer lenders using internet platforms; and
- Regulatory constraints on MFIs as well as microenterprises (taxes, licenses, etc.).

Aside from its relatively limited reach, microfinance in the US differs significantly from that in the developing world. Major differences include:⁸¹

- While loan amounts in the developing countries are typically very small (average \$500), loans in the U.S. may be up to \$50,000;
- Interest rates on microloans in the U.S. are typically much lower than in developing countries;
- In the U.S., loans are usually for microenterprise creation and operation, while MFIs in developing countries lend for a broader range of purposes, to include consumer goods or general consumption;

⁷⁸ Page iv. <https://www.newyorkfed.org/medialibrary/media/smallbusiness/2015/Report-SBCS-2015-Nonemployer-Firms.pdf>

⁷⁹ Additionally, banks and other formal financial institutions may be reluctant to lend small amounts even to qualified borrowers due to the attendant administrative costs – small loans consume the same administrative resources as large loans without the same return on investment.

⁸⁰ See Schreiner and Morduch (2001, 8-18); Servon (2006, 353); Sengupta and Aubuchon (2008, 25-26); Gomez and Edgcomb (2011, 5-8); Chandra and Arun (2011, 2); Lieberman *et al* (2012, 34); and Bernstein (2014, 88-89).

⁸¹ See Lieberman *et al* (2012, 34-37); Hoy *et al* (2012); Chandra and Arun (2011, 16-17); Servon (2006); Burrus (2005); California Association for Micro Enterprise Opportunity (CAMEO) <http://www.microbiz.org/about-micro-business/microlending-2/microlending-faq/#interest>; and ACCION EAST <http://www.accioneast.org/home/support-action/learn/microlending-in-the-united-states.aspx>.

- Business training or technical assistance are available to the borrower in the U.S., or are a condition of receiving the loan;⁸²
- U.S. MFIs typically do not use group-liability or collective responsibility in lending, as is done in many developing countries;⁸³ and
- MFIs in the U.S. generally have higher operating costs, driven by employee salaries, training services, in pursuit of financial support and compliance with support conditions.

In their 2012 report on microfinance in the U.S., Lieberman *et al* (2012, 36) assessed the industry's ability to scale up services to the underserved and become self-sustaining. They concluded that:

"U.S. programs remain reliant on a limited supply of heavily subsidized funding from government, private for-profit, and non-profit sources, owing to the high cost of acquiring clients, the necessary emphasis on training provided at little or no charge, higher operating costs, and the inability to price loans at interest rates that cover expenses. Thus, microfinance programs in the United States are far more expensive to maintain, slower to expand, and much less likely to reach 100% financial self-sufficiency than their developing-country MFI counterparts."

Public funding for MFIs comes from a variety of federal, state and local sources. Most federal funding is provided through two programs: The Community Development Financial Institution Fund (CDFI Fund) of the U.S. Department of the Treasury;⁸⁴ and the U.S. Small Business Administration's Microloan Program.⁸⁵ Sources of private funding include foundations, social investment funds, religious organizations, and individual donors. While important sources of capitalization, these funding sources come with conditions that may constrain MFIs – principally interest caps and administrative requirements that may prevent cost recovery.⁸⁶

To a limited extent, for-profit MFIs have developed niche markets⁸⁷ in microcredit, typically as one component in a broader array of other financial services.⁸⁸ These emerging MFIs typically charge higher interest rates than non-profits, unless constrained by donor conditions.

In summary, microfinancing in the U.S. focuses on providing microcredit, training, building wealth for the borrower and advancing them into the mainstream financial community.

⁸² Lieberman *et al* (2012, 35) note that "(t)o a large degree, regulatory requirements also drive the much greater need for training in the United States."

⁸³ For a discussion of group-liability and enforcement issues, see Sherratt (2016, 71-86).

⁸⁴ <https://www.cdfifund.gov/Pages/default.aspx> Also See Lieberman *et al* (2012, 43).

⁸⁵ <https://www.sba.gov/loans-grants/see-what-sba-offers/sba-loan-programs/microloan-program> For links to SBA-Accredited Microloan programs, by state, see <https://www.powerhomebiz.com/microloan-providers> Also See Lieberman *et al* (2012, 42).

⁸⁶ Lieberman *et al* (2012, 44).

⁸⁷ For example, a number of for-profits market to immigrant communities or ethnic groups.

⁸⁸ Lieberman *et al* (2012, 59-66). For example, OUR Microfinancing in SE Florida is a certified CDFI which offers "small, short-term loans for small businesses, as well as other financial services like Investment, Technical Assistance, and Equipment Leasing." <http://ourmicrolending.com/> Also See Gomez and Edgcomb (2011) and Assanie and Virmani (2006).

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Appendix Two: STATE SUPPORT FOR FLORIDA SMALL AND STARTUP BUSINESSES

Introduction

Historically, the State of Florida has funded a variety of strategies to promote economic growth, including:

- Promotion of Florida tourist destinations and industries;
- Providing grants, tax refunds, tax credits and tax exemptions to specific businesses or targeted industries to induce retention, relocation to or expansion in the state;
- Recruiting foreign direct investment and providing export assistance to Florida businesses;
- Providing subsidies to businesses for redevelopment or investment in targeted geographic areas in the state.

Another component of the state's strategy is to offer or support a variety of programs that provide financial or technical assistance to small and "startup" businesses. This Appendix provides an overview of Florida's financial and technical assistance programs for small businesses; venture capital and state-funded venture capital strategies; and Florida's venture capital programs.

What is a "Small Business?"

Definitions of what qualifies as a "small business" vary among state and federal programs, considering a number of factors that include the number of employees, assets, and revenues. For most programs offered by Florida, a small business is defined as:

"... an independently owned and operated business concern that employs 200 or fewer permanent full-time employees and that, together with its affiliates, has a net worth of not more than \$5 million or any firm based in this state which has a Small Business Administration 8(a) certification. As applicable to sole proprietorships, the \$5 million net worth requirement shall include both personal and business investments."⁸⁹

The U.S. Small Business Administration (SBA) has "established two widely used size standards – 500 employees for most manufacturing and mining industries and \$7.5 million in average annual receipts for many nonmanufacturing industries," as qualifying criteria for financial assistance programs it offers. However, exceptions to this standard apply for many industries.⁹⁰ The Census Bureau, the Bureau of Labor Statistics, and the Federal Reserve use the SBA standards.

TABLE 1 shows the range of business size in Florida, as measured by number of employees.

What is a "Startup?"

A 'startup' is a small business in an early stage of an enterprise "where the entrepreneur moves from the idea stage to securing financing, laying down the basic structure of the business, and initiating operations or trading."⁹¹ Serial entrepreneur Steve Blank describes a startup as a "temporary

⁸⁹ Section 288.703(6), F.S. For state agency rule-making purposes, s. 120.54(3)(b)2.a., F.S., allows inclusion of businesses with more than 200 employees under specified circumstances.

⁹⁰ See <https://www.sba.gov/content/summary-size-standards-industry-sector> and <https://www.sba.gov/category/navigation-structure/contracting/contracting-officials/small-business-size-standards>

⁹¹ <http://www.businessdictionary.com/definition/startup.html#ixzz3pQP4y3sy>

Investopedia defines a startup as

organization designed to search for a repeatable and scalable business model, with the intention of becoming a large business.”⁹²

TABLE 1
Florida Businesses, per Number of Employees

Employment Range	Firm		Employment	
	Percent of Total	Cumulative Percent	Percent of Total	Cumulative Percent
Fewer than 5	71.7%	71.7%	6.1%	6.1%
5 to 9	12.7%	84.4%	5.2%	11.3%
10 to 19	7.4%	91.8%	6.2%	17.5%
20 to 49	4.8%	96.6%	9.0%	26.5%
50 to 99	1.6%	98.2%	7.0%	33.5%
100 to 249	1.1%	99.3%	10.1%	43.6%
250 to 499	0.4%	99.7%	7.7%	51.3%
500 to 999	0.2%	99.9%	8.1%	59.4%
1,000 or more	0.2%	100.0%	40.7%	100.0%

Source: Florida Department of Economic Opportunity, Labor Market Statistics Center, received July 31, 2017. Data are for March 2016.

Florida’s Financial Assistance Programs for Small Businesses

There are several state-funded or state-supported programs available in Florida to provide financial assistance targeted to small businesses, including loans, loan support, and loan assistance.

In 2014, the Florida Legislature enacted the “Florida Microfinance Act,”⁹³ to create the Microfinance Loan and Microfinance Guarantee programs through the Department of Economic Opportunity (DEO) to increase access to credit for entrepreneurs and small businesses in Florida.

The **Microfinance Loan Program**⁹⁴ provides funding of up to fifty percent of fixed-rate, short-term loans (one year or less), not to exceed \$50,000, to qualified Florida businesses with 25 employees or fewer and gross annual revenues of \$1.5 million or less per year for the last 2 years. Loan administrators are required to reserve ten percent of the program funds for businesses that employ less than six people and generate annual gross revenues of less than \$250,000 per year for the last 2 years. A borrower is limited to no more than two microloans per year, not to exceed a total of \$75,000, and no more than five microloans in any 3-year period.⁹⁵ Loans are only available for startup costs, working capital, and the acquisition of materials, supplies, furniture, fixtures, and equipment.⁹⁶ Loans are capped at the current

“... a company that is in the first stage of its operations. These companies are often initially bank rolled by their entrepreneurial founders as they attempt to capitalize on developing a product or service for which they believe there is a demand. Due to limited revenue or high costs, most of these small scale operations are not sustainable in the long term without additional funding from venture capitalists.”

<http://www.investopedia.com/terms/s/startup.asp>

⁹² <https://blog.generalassembly.ly/difference-between-a-startup-and-a-small-business/>

⁹³ Sections 49 - 57, ch. 2014-218, L.O.F.

⁹⁴ Section 288.9934, F.S. <http://www.floridajobs.org/business-growth-and-partnerships/for-businesses-and-entrepreneurs/business-resources/florida-microfinance-program>

⁹⁵ Section 288.9934(9)(d), F.S. The total cap for a three-year period would be \$200,000.

⁹⁶ Section 288.9934(9)(b), F.S., imposes specific restrictions on use of loan proceeds.

prime rate plus 1000 basis points.⁹⁷ As a condition of receiving the loan, the borrower “must participate in business management training, business development training, and technical assistance,” as determined by the loan administrator, through the network of Florida Small Business Development Centers (SBDCN Centers).⁹⁸

Through FY 2016-17, \$1,345,407 in state funds (26.25 percent of the total \$5,125,000 allocation) has been loaned to businesses through the Loan Program. Two entities are under contract to administer the loan program: the Florida Black Business Support Corporation⁹⁹ and OUR MicroLending, LLC.¹⁰⁰ At the end of their three year contracts, the loan administrators are to remit the state portion of the principal from all repaid loans to DEO.¹⁰¹

The **Microfinance Guarantee Program**¹⁰² backs loans by private lenders to Florida businesses. Like the microloan program, eligibility is limited to businesses with 25 employees or fewer and gross annual revenues of \$1.5 million or less per year for the last 2 years. Guarantees are limited to loans of \$50,000 to \$250,000, and may not exceed fifty percent of the total loan amount.¹⁰³ Through FY 2016-17, \$841,639 (17.4 percent of the total \$4,825,000 allocation) has been used to support loans to businesses through the Guarantee program. As required by law, DEO contracts with Enterprise Florida, Inc. (EFI) to administer the program.

Together, these programs received \$10 million in nonrecurring funds in 2014, with the intention that such funds be reinvested and maintained as a long-term and stable source of funding for these programs.¹⁰⁴

The federal Small Business Jobs Act of 2010 created the **State Small Business Credit Initiative** (SSBCI) to strengthen state programs that support lending to small businesses. SSBCI was funded with \$1.5 billion which was allocated among 57 states, territories, and local governments, to be used in new or existing small business development programs.¹⁰⁵ Florida was granted \$98 million of SSBCI funding, which is being used in four state programs. The Florida Loan Support Program and the Florida Capital Access Program were newly created to take advantage of SSBCI funding, while the Florida Export Finance

⁹⁷ Section 288.9934(9)(d)6., F.S. On May 31, 2017, the capped interest rate was 14 percent. Loan administrators report loan interest rates from 13.25 to 14 percent.

⁹⁸ DEO reports that the SBDCN uses “Profit Mastery,” a training and technical assistance curriculum which includes six modules and provides applicants with financial literacy skills and business management training necessary for small business success. The Florida SBDCN provides entrepreneurial and business development services in 46 communities throughout the state. See <http://floridasbdc.org/Main.php> for additional information.

⁹⁹ The Florida Black Business Support Corporation dba Access Florida Finance Corporation provides financing to Florida’s small business owners. <http://www.accessfloridafinance.com/microfinance-loan-program/>

¹⁰⁰ OUR MICROLENDING is a Community Development Financial Institution that offers an alternative financial service for entrepreneurs whose needs are not met by regular banking institutions. <http://ourmicrolending.com/>

¹⁰¹ Section 288.9934(6)(a), F.S. While s. 288.9934(4)(a), F.S., infers the loan program will “be maintained as a long-term and stable source of funding for the program,” (3)(a) does not specifically authorize a subsequent round of awards to program administrators at the end of the initial three-year contracts.

¹⁰² Section 288.9935, F.S. <http://www.floridajobs.org/business-growth-and-partnerships/for-businesses-and-entrepreneurs/business-resources/florida-microfinance-program>

¹⁰³ However, the loan to guarantee ratio may not exceed 3:1.

¹⁰⁴ Section 288.9934(4)(a) and 288.9935(1), F.S. To date, \$56,317 has been allocated for marketing-related expenses.

¹⁰⁵ For a recent review of the SSBCI Initiative, see “Program Evaluation of The US Department of Treasury State Small Business Credit Initiative,” Prepared by the Center for Regional Economic Competitiveness and Cromwell Schmisser, October 2016. This report summarizes the outcomes of 142 state credit support and investment programs funded by the SSBCI.

https://www.treasury.gov/resource-center/sb-programs/Documents/SSBCI_pe2016_Full_Report.pdf

Corporation and the Florida Opportunity Fund already existed in the state and are using SSBCI funds to expand the number of loans to small businesses.¹⁰⁶

The **Florida Loan Support Program** was created in Enterprise Florida, Inc. (EFI) and allocated \$47.2 million in SSBCI funds to:

“...assist small businesses in obtaining loan approvals and leverage private capital for use in startup costs, working capital, business procurement, franchise fees, equipment, inventory, or the purchase of owner-occupied commercial real estate. The program provides a lender with the necessary security, in the form of a partial guarantee, for the lender to approve a loan or line-of-credit.”¹⁰⁷

Rather than provide direct loans to businesses, the program offers partial loan guarantees or loan participations to lenders that make loans to businesses. Guarantees and participations range between \$250,000 and \$500,000, from five to fifty percent of the loan amount.¹⁰⁸

SSBCI funds were also used to create and capitalize the **Florida Capital Access Program (CAP)**, a “loan portfolio insurance program that allows lenders to make loans to small businesses that are creditworthy but may not otherwise have access to credit.”¹⁰⁹ A loan loss reserve fund insures a portion of each loan. The CAP insurance is matched by the participating financial institution loan loss reserve fund, which is supported by fees from the lender and borrower. The program is administered by the Department of Economic Opportunity (DEO) using \$2 million of the federal SSBCI funds. Florida businesses with fewer than 500 employees are eligible for a loan of up to \$5 million, and loan proceeds must be used for a business purpose.

The Florida Loan Support and the Florida Capital Access Programs are similar to the Microfinance Loan and Loan Guarantee programs, except that the SSBCI programs have “a stated minimum loan size of \$250,000 and as such, tend to complement rather than compete with the Microfinance Programs.”¹¹⁰

The **Florida First Capital Finance Corporation (FFCFC)** was established and initially capitalized by the Florida Legislature in 1983 and, until 2002, was under contract with the State Department of Commerce to promote and assist the growth and development of small businesses in the state.¹¹¹ Among other services, the FFCFC assists businesses through the U.S. Small Business Administration’s (SBA) 504 Loan Program, which provides “affordable long-term capital for the purchase of major fixed assets, such as owner-occupied commercial real estate, energy efficient “green” initiatives, and/or heavy duty

¹⁰⁶ “Evaluation of the State Small Business Credit Initiative,” Office of Economic and Demographic Research of the Florida Legislature, 1/1/15. Page 1. <http://edr.state.fl.us/Content/returnoninvestment/SSBCIReportFinal.pdf>
https://www.treasury.gov/resource-center/sb-programs/Documents/SSBCI_pe2016_Full_Report.pdf

¹⁰⁷ <http://www.enterpriseflorida.com/small-business/>

¹⁰⁸ <https://www.enterpriseflorida.com/small-business/state-small-business-credit-initiative-ssbci/>

¹⁰⁹ “Evaluation of the State Small Business Credit Initiative,” Office of Economic and Demographic Research of the Florida Legislature, 1/1/15. Page 6. <http://edr.state.fl.us/Content/returnoninvestment/SSBCIReportFinal.pdf>

Also See: [&](http://sitefinity.floridajobs.org/business-growth-and-partnerships/for-businesses-and-entrepreneurs/business-resources/small-business-programs/state-small-business-credit-initiative/florida-capital-access-program)
http://sitefinity.floridajobs.org/Community/SSBCI_CAPPowerPoint.pdf

¹¹⁰ Microfinance Programs Annual Report, 2017. Division of Community Development, Florida Department of Economic Opportunity, November 1, 2016, p. 3. <http://www.floridajobs.org/docs/default-source/reports-and-legislation/microfinanceannualreportfy16-17.pdf?sfvrsn=2>

¹¹¹ Section 288.7011, F.S., repealed by s. 486, ch. 2011-142, L.O.F. <https://fffcfc.com/about-us-2/about-florida-first-capital/>

machinery and equipment, without the high down payment requirements often associated with conventional financing programs”¹¹²

Technical Assistance Programs for Small Businesses

Florida supports a number of programs that provide technical assistance to small businesses. The **Economic Gardening Technical Assistance Program**, administered by GrowFL, provides strategies, resources, and support to second stage companies seeking to expand their businesses. To qualify for assistance, businesses must be Florida-based, for-profit companies that employ between 10 and 50 persons, generate between \$1 million and \$25 million in annual revenues, have experienced steady growth in gross revenues and employment during 3 of the last 5 years, and be eligible for the Qualified Targeted Industry tax refund program. The program has been appropriated a total of \$5.5 million since 2009.¹¹³

The **Florida Small Business Development Center Network** (Network) is designated by the Florida Legislature as “the principal business assistance organization for small businesses in the state.”¹¹⁴ Network affiliates provide “professional expertise, tools, and information” to “entrepreneurs in every stage of the business life cycle.”¹¹⁵

The Network was established in 1976 pursuant to the Small Business Act (15 U.S.C. § 648) as a partnership between the U.S. Small Business Administration (SBA) and the post-secondary education system to provide business management and educational assistance directly to small businesses. The Network consists of eight affiliated Small Business Development Centers (SBDCs) and 45 offices located throughout the state, which are managed by the Lead Center at the University of West Florida (UWF). The Lead Center, in addition to serving its local small business community, is also responsible for administering the activities of the Network through memoranda of understanding with each affiliated SBDC. The eight SBDCs are housed within UWF, Gulf Coast State College, Palm Beach State College, the University of North Florida, The University of Central Florida, The University of South Florida, Florida Gulf Coast University, and Florida Agricultural and Mechanical University.

Funding for the Network is supplied from federal, state, local, and private sources, including both cash and in-kind contributions. All federal funds must be matched through cash, indirect, and in-kind contributions. SBDC services are targeted to the needs of businesses with fewer than 100 employees. These services include providing information or research, consulting, educating, or assisting businesses with:

- Planning related to startup, operation, or expansion of a small business enterprise;

¹¹² <https://fffcfc.com/loan-programs/the-sba-504-loan-program/the-sba-504-loan-program-overview-eligibility>

The SBA offers two additional programs available through other organizations. The 7(a) Loan Program provides financing for long- or short-term working capital needs, inventory and equipment purchases, expansion/renovation, business start-up or existing debt refinancing under certain specific conditions. The Microloan Program provides loans up to \$50,000 to help small businesses, through four designated intermediary lenders in Florida.

See <https://www.sba.gov/loans-grants/see-what-sba-offers/sba-loan-programs/microloan-program>

For a list Florida institutions offering SBA microloans, see: <https://www.sba.gov/sites/default/files/articles/microlender rpt2.pdf>

¹¹³ Section 288.1082, F.S. Section 54, ch. 2009-1, L.O.F., appropriated \$10 million to fund both the Economic Gardening Technical Assistance and Loan programs. The loan program has expired. The program also received \$2 million in FY 2012-13.

See <http://www.growfl.com/> and DEO’s Annual Report, FY 2016-17, page 22 @ <http://www.floridajobs.org/docs/default-source/reports-and-legislation/2017-deo-annual-report.pdf?sfvrsn=2>

¹¹⁴ Section 288.001(1), F.S.; ch. 2013-39, L.O.F.

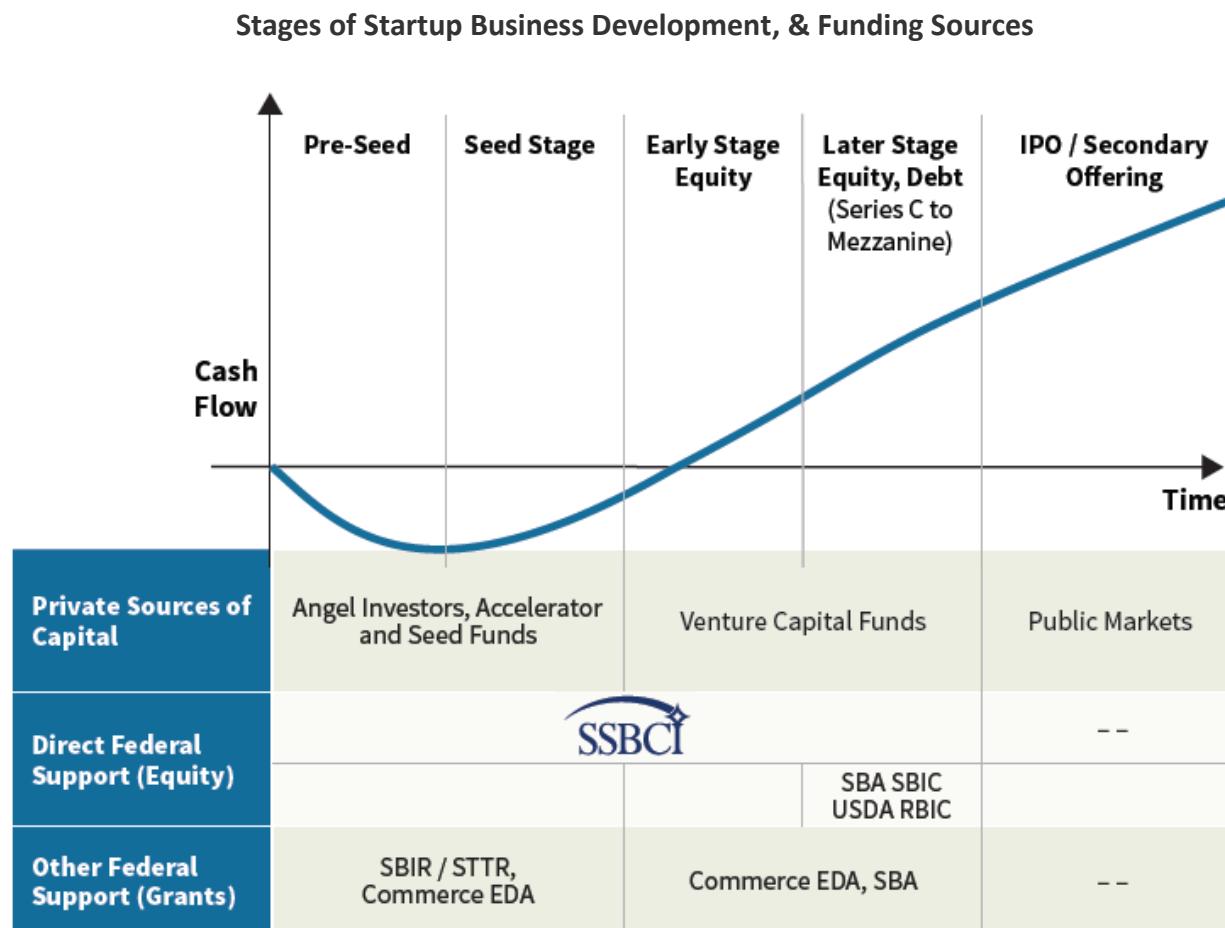
¹¹⁵ <http://floridasbdc.org/>

- Developing and implementing strategic or business plans;
- Developing the financial literacy of existing businesses related to their business cash flow and financial management plans;
- Developing and implementing plans for existing businesses to access or expand to new or existing markets;
- Supporting access to capital for business investment and expansion; and
- Assisting existing businesses to plan for a natural or man-made disaster, and assisting businesses when such an event occurs.

SBDCs also provide assistance related to international trade and exporting; e-commerce; technology transfers; disaster recovery compliance with federal regulations; and market research.¹¹⁶

Overview of Venture Capital

Startups require various and complementary types of capital throughout their stages of development, as illustrated in this chart from Cromwell and Schmisseur (2016, 13):



Source: Cromwell Schmisseur (2016, 86), used by permission. For information regarding Federal support through these stages, see pp. 85-86.

¹¹⁶ This summary of the SBDC was adapted from a bill analysis for HB 7007, 2013, Economic Development and Tourism Subcommittee of the Florida House of Representatives, pp. 14-16, 4/22/13.

Pre-seed capital finances the research to develop the idea or “prove the concept that demonstrates the potential value of their intellectual property.”¹¹⁷ **Seed stage** businesses generally “have the founding team working to develop product prototypes or business model concepts.”¹¹⁸ Sources of funding for these investments include the individual entrepreneur, friends and family, business accelerators, research institutions, public research centers, government-supported seed-funds, investment partnerships, private corporations, and individual or Angel investors. As Heard and Sibert explain (2000, 10), a typical Angel investor:

“...is a high-net worth individual with an interest and knowledge in a particular business sector, often because that is where he or she gained personal wealth. Angels can help a start-up company with their considerable experience... An angel will frequently become an active advisor to the company and often take a seat on its board of directors.”¹¹⁹

Venture capital (VC) is capital invested in early and growth stages of the business, typically in which there is a substantial element of risk.¹²⁰ Tarpe (2012, 2) describes VC as:

“...financial capital – money – provided to startup companies with extraordinary growth potential. Companies and managers that work with venture capital – “venture capitalists” – are essentially financial intermediaries that raise money from wealthy individuals, corporations and institutional funds (e.g. pensions) and invest them in privately-held companies. As a general rule, venture capitalists invest in the early stages of a company, with the goal to turn sizable profits as its value increases several fold. In exchange for their capital, venture capitalists typically take an ownership stake in selected companies and closely monitor, if not directly influence, company decision-making.”

Citing Kaplan and Stromberg (2001) and Gompers and Lerner (2001), Gompers et.al, (2016, 2) note that Venture Capitalists “are particularly successful at solving an important problem in market economies – connecting entrepreneurs with good ideas (but no money) with investors who have money (but no ideas).” Gornall and Strebulaev (2015, 2) characterize venture capital as:

“...a high-touch form of financing used primarily by young, innovative, and risky companies... Venture capitalists provide not only financing, but also nonfinancial support such as mentorship, strategic guidance, and network access. VC investments are typically highly speculative. While most VC-funded companies fail, some become runaway successes.”

So, Venture Capitalists not only provide funding to startups with promising innovations, they also provide management expertise to guide entrepreneurs in the development of the products and services, and the successful development of the business. Venture capital investments typically involve

¹¹⁷ Cromwell Schmisssieur (2016, 74).

¹¹⁸ *Ibid*, 74-75.

¹¹⁹ *Also See*: Lerner and Schoar (2016).

¹²⁰ The term Venture Capital is sometimes used broadly, to include seed capital investments. Also, venture capital may be considered as a type or subset of private equity (PE), in that both investments are in companies that are not publicly traded on a stock exchange. However, VC is distinguished from PE by the type of company invested in: typically, PE investments are in existing companies while VC investments are typically in new products developed by new businesses with very little capital. As such, these investment are considered substantially riskier. See

<https://www.forbes.com/sites/victorhwang/2012/10/01/presidential-debate-primer-whats-the-difference-between-private-equity-and-venture-capital/#177be8513c45>

concurrent equity participation in multiple businesses with a 5 to 10-year time horizon for exiting the investments.¹²¹

State-Funded Venture Capital Strategies

State venture capital programs “are part of a broader economic development strategy to promote entrepreneurial activity on the theory that innovation and entrepreneurship drive long-term economic growth and diversification.” (Cromwell and Schmisseur, 2016, 61)

It was recently reported that seventy-seven percent of venture capital in the US is going to four metropolises: Silicon Valley, New York, Boston and Los Angeles.¹²² Venture Capitalists generally require proximity to their investments. Consequently, they recruit within their region or, in many cases, require out-of-state startups to relocate as a condition of investment. In 2001, Barkley, Markley and Rubin (2001, 350) observed that:

“The geographic concentration and industrial focus of venture capital investments have contributed to the perception that specific regions of the country (the more geographically isolated and/or sparsely populated) and certain industries (traditional, non-high tech) are underserved by private venture capital firms. A common response to this perception of a venture capital shortage is the initiation of public programs to enhance the availability of equity capital for local entrepreneurs and businesses.”

States have responded with a number of strategies, including granting tax credits for equity investments in qualifying businesses, or qualified seed funds or venture capital funds. In 2014, Gullickson (2014, 12) reported that “(t)here are twenty-nine states that have, at some point, encouraged the growth of venture capital through the use of tax credits. Five states have either allowed their credit to sunset or the tax credit has been repealed.” A recent report of the National Conference of State Legislatures (NCSL 2014, 8) offered this perspective on such state tax credit programs:

“Many economists are skeptical of the value of angel and venture capital tax credits, arguing that they are based on the unproven assumptions that the private sector is under-investing in new businesses and that tax credits will counteract that underinvestment. They claim that tax credits would rarely entice someone to make an investment who otherwise would not. And at the same time, tax credits won’t make angels invest in a company that they wouldn’t invest in without the credit. A bad investment is a bad investment, and while angels are risk-takers, most

¹²¹ Barkley, DiFurio and Leatherman (2000, 84) describe how venture capital funds are typically organized:

The managing partners generally receive an annual management fee of 2-3 percent of fund capital and a predetermined percentage of the profits on the fund’s investments (for example, 20 percent). The original investment in the fund by the limited partners and the remaining gains on the portfolio investments (for example, 80 percent of the profits) are returned to the limited partners. In sum, limited partnerships incorporate the structure, incentives, and checks and balances necessary to encourage a common goal (maximize the rate of return on fund investments) for the investors, managing partner, and portfolio companies. This type of traditional venture capital institution is considered a relatively efficient means of raising funds from investors and allocating these funds among investment alternatives.

¹²² Liner, Emily and Ryan Bhandari. “America’s Got Talent -- Venture Capital Needs to Find It.” Third Way, Feb. 16, 2017.

<http://www.thirdway.org/report/americas-got-talent-venture-capital-needs-to-find-it>

Horwitz, Gabriel. “Does VC Mean Venture Capital Or Very Concentrated? Washington Bytes, Forbes, Feb., 16, 2017, pp. 6-8.

<https://www.forbes.com/sites/washingtonbytes/2017/02/16/does-vc-mean-venture-capital-or-very-concentrated/#9391c3577e38>

For timely information regarding VC investments, see <http://www.pwc.com/us/en/technology/moneytree.html>

of them won't throw their money away because someone waves an incentive in front of them. Others argue that the investment would likely have happened anyway and that tax credits simply reward investors for investments they are making anyway. As a result, tax revenues decline but no new investment occurs in response to the credit. In addition, a tax credit may not increase the number of companies receiving new money. Because tax credits don't improve the quality of the unfunded deals, investors might remain focused on the deals they were willing to make without the credit. In this case, tax credits might attract more investors to the same deals, leading not to more companies getting funded, but to competition for deals, which could increase valuations and reduce returns."

Cromwell and Schmisser (2014, 18-19) identify three additional state-funded venture capital strategies or programs: Direct Investment Funds, Fund-of-Funds and Certified Capital Companies (CAPCOs).

Direct Investment Funds invest public funds in individual startups, sometimes in specified industries or with targeted social objectives. Cromwell and Schmisser (2015, 1) note that such funds managed by state employees "are rare, with most programs managed by private investors or private nonprofit corporations with credible teams." The NCSL (2014, 6) noted that this strategy has many detractors who argue that direct investment in startups "is not an appropriate role for state government and the risky nature of venture capital is an unacceptable use of public funds."

In **Fund-of-Funds** programs, states invest in institutional venture capital funds, which allows these states to benefit from the fund managers' access and expertise. In most programs, state funds (or a percentage of state funds) are restricted to investments in in-state startups. Also, the programs are designed to be self-sustaining – the state's portion of the profits are reinvested in subsequent funds. Barkley and Markley (2001, 22) note that "(i)n public/private venture capital programs, the State sacrifices control over investment decisions (and social objectives) in return for the more limited financial risk associated with private, professionally managed funds."

At least eight states and the District of Columbia have implemented **Certified Capital Company** (CAPCO) programs since 1988.¹²³ Schmisser and Overmoyer (2010, 2-3) describe the template for CAPCO programs this way:

"CAPCO funds create a complex structured finance product that converts future tax credits into funds that can be invested in small businesses today. An insurance company that "invests" in the CAPCO security will receive deferred tax credits equal to the amount of the investment. The tax credits can be used in future years... Additionally, the insurance company investors will receive the principal and interest from U.S. Treasury securities purchased with nearly half of their invested funds and held in escrow until the securities mature. The combination of the future tax credits and the escrow fund proceeds provide the insurance companies with a fixed income return that is guaranteed by a kind of default insurance referred to as the "wrap," which is also purchased by the CAPCO funds from the investor proceeds.

...

What most lawmakers do not understand is that the CAPCO program consumes the entire amount of the state taxpayer investment ... The state commits the capital, insurance company

¹²³ Louisiana (1988), Missouri (1997), New York (1998), Wisconsin (1999), Florida (1999), Colorado (2002), Alabama (2004), Texas (2005) and Washington D.C. (2005). Tennessee has TNInvestco, which Krumm (2010, 118 & 123) characterizes as Tennessee's modified version of a CAPCO. Florida's CAPCO program was repealed in 2010. [Section 1, Ch. 2005-91., L.O.F.]

investors get a fixed-income return, and small businesses get capital investments for which they must pay back the principal plus interest and/or give up equity in their companies. Once the CAPCO funds have met their statutory requirements, the fund is “decertified” and the fund owners keep everything left over.”

In comparing CAPCOs to traditional venture capital funds, Dr. Julia Sass Rubin, Associate Professor at Rutgers Bloustein School of Planning and Public Policy, notes that:

Normal venture capitalists make their money from the profits they earn for their investors. If they make smart investments, they keep 20 percent of the profits. In all cases, however, they must return all of the original investment capital to their investors. By contrast, CAPCO managers get to keep almost all of the profits plus the money that they invest...¹²⁴

In their review of the Texas CAPCO program, the Texas Legislative Budget Board (2013, 106) suggested that “(i)f the CAPCO program were structured like a traditional venture capital investment, the successful CAPCOs would return the state’s initial investment and a portion of CAPCO profits. This arrangement would provide an ongoing source of venture capital for the state.”

Cromwell and Schmisser (2014, 19) offer this perspective on state CAPCO programs:

“More than \$2 billion of state capital has been invested in CAPCO models in the past 20 years... In some states, programs provide for a nominal share of investment profits to accrue to the state, but importantly, the state loses ownership rights to the investment principal derived from the tax credits. CAPCO programs have been widely criticized for unfair economics, excessive financing costs, investments structured as loans to mature companies and disputed job creation claims. If the stated goal is to support and increase venture capital investment, this model is not recommended.”

Cooper, Barkley and Williams (2001, 3) echo this recommendation, concluding that CAPCOs “are identified as by far the most expensive model to facilitate the formation of venture capital.”¹²⁵

Cromwell and Schmisser (2015, 1) offer a “best principles” framework for state venture capital programs:

- Efficiently finance state capital programs for small business investments and consider aligning state fiscal impact with comprehensive economic development impact;
- Invest in/with legitimate venture investors selected via a competitive selection process;
- Restrict investments to address identified small business financing gaps not adequately served by the private sector (equity and debt capital sources); and
- Require a market-standard return of capital invested (100% of principal and majority % of profits) when utilizing for-profit managers so that state interests are aligned with private investors and capital is returned for ongoing support of a state’s innovation economy.

¹²⁴ <http://prowlingowl.com/Scams/CAPCO/100millionRIScam.cfm>

¹²⁵ While economic impact studies commissioned by program proponents find otherwise, reports of state auditors and research conducted by independent analysts (academics and analysts working independent of program proponents), consistently find that CAPCO programs are not cost-effective, fall short on promised economic impact, and are a poor strategy to increase venture capital investments in startup businesses. See Reference section for links to evaluations of State CAPCO programs.

Major State Initiatives

A few states have implemented significant public-funded initiatives that provide VC or access to VC, and related support services and assistance to entrepreneurs. Ohio's \$2.1 billion Ohio Third Frontier¹²⁶ offers:

- The Entrepreneurial Services Provider Program, which established networks of entrepreneurial services and capital to accelerate the growth of early stage Ohio technology companies;
- The Technology Validation and Start-up Fund, which provides funds to commercialize technologies developed by Ohio research institutions; and
- The Pre-Seed/Seed Plus Fund Capitalization Program increases the availability of professionally managed capital and associated services for early stage Ohio technology companies.

Michigan offers four different venture capital programs, with a cumulative investment (public and private) of over \$500 million. One program is the Venture Michigan Fund I & II (VMF). A unique feature of this fund-of-fund is that the fund capital is raised by outside investors, with the state offering to provide investors a guarantee with up to \$200 million in tax voucher certificates to offset any shortfall in debt servicing.¹²⁷

In 2005, Texas created the Texas Emerging Technology Fund to provide early stage technology funds, research award matching grants, establish "Regional Centers of Innovation and Commercialization" and recruit research talent for Texas universities. Over its ten-year active existence, \$400 million was appropriated to the Fund.¹²⁸

Florida's Venture Capital Programs

There are a variety of state-funded or state-supported programs available in Florida to provide venture capital and technical assistance to startup businesses. Venture capital is invested directly in qualified Florida businesses, or indirectly through a "fund of funds" strategy. Technical assistance is available for commercializing both public and private research, directly through state funded programs or indirectly through publicly-supported business incubators. Florida also assists startups in accessing public and private financial resources to enable their expansion.¹²⁹

In 2007, the Legislature created within Enterprise Florida, Inc. (EFI) the **Florida Opportunity Fund** (FOF) to increase the availability of seed capital and early stage venture equity capital for Florida startups. The FOF was originally created as a "fund of funds" program for the purpose of investing in seed and early stage venture capital funds managed by managers with demonstrated experience, expertise, and a successful history of investing venture capital funds, with a focus on venture capital opportunities in Florida. In order to receive an investment from the FOF, a venture capital fund must demonstrate a record of successful investment in Florida, be based in the state, or have an office staffed with a full-time, professional venture investment executive. Funds must have raised capital from other sources of

¹²⁶ Ohio Third Frontier was implemented in 2002, and extended in 2010.

http://development.ohio.gov/b3_thirdfrontier/default.htm

¹²⁷ <http://www.michiganbusiness.org/grow/access-capital/#section1-2>

¹²⁸ The Fund was abolished in 2015, with assets and management responsibilities were transferred to the Texas Treasury Safekeeping Trust Company. <http://www.govtech.com/state/Texas-Gov-Abbott-Abolishes-Rick-Perrys-Emerging-Tech-Fund.html> and

<http://www.siliconhillsnews.com/2015/10/21/texas-emerging-technology-fund-still-benefiting-life-sciences-startups/>

¹²⁹ Unlike many other states, Florida does not offer tax credits for equity investments in qualified businesses. Florida's CAPCOs program was repealed in 2010.

at least twice the FOF's investment. The Legislature provided an initial appropriation of \$29.5 million from the General Revenue Fund for FOF's venture capital investment efforts.¹³⁰

The scope of the FOF's purpose was expanded in 2009 to allow it to provide direct investments in and loans to businesses and infrastructure projects that are Florida-based and operate in technology sectors that are strategic to Florida.¹³¹ In order to receive a direct investment, a business or infrastructure project must have raised capital from other sources of at least twice the FOF's investment.

In 2010, the **Clean Energy Investment Program** was established within the FOF, with \$36,089,000 in funding by the US Department of Energy through the American Recovery and Reinvestment Act of 2009 (ARRA) to the Florida Department of Agriculture and Consumer Services' Office of Energy. These funds are designated to "promote the adoption of energy efficient and/or renewable energy (EE/RE) products and technologies in Florida by providing funding to businesses to increase the use of EE/RE technologies, equipment and materials in the State."¹³² Program funds are used for direct investments in qualified businesses.

In 2012, the **Florida Venture Capital Program** was established within the FOF and allocated \$43.5 million in SSBCI funds to invest in Florida-based companies.¹³³ To qualify for direct investment, a business must fall within EFI's designated target industries and have fewer than 500 employees.¹³⁴

EFI also administers the **Florida Small Business Technology Growth Program**, established in 1998 to "provide financial assistance to businesses in the state having high job growth and emerging technology potential and fewer than 100 employees."¹³⁵ The program was capitalized with \$1.5 million,¹³⁶ and authorized use of the funds include "loan guarantees, letter of credit guarantees, cash reserves for loan and letter of credit guarantees, payments of claims pursuant to contracts for guarantees, subordinated loans, loans with warrants, royalty investments, equity investments, and operations of the program."¹³⁷

Another potential source of venture capital for startups is the **Florida Growth Fund**, implemented in 2008 by the State Board of Administration (SBA).¹³⁸ Section 215.47(7), F.S., authorizes the SBA to invest 1.5 percent, or approximately \$1.1 billion, of the net assets from the system trust fund "in technology and growth investments of businesses domiciled in this state or businesses whose principal address is in

¹³⁰ Chapter 2007-189, L.O.F., codified as s. 288.9624, F.S. <http://www.floridaopportunityfund.com/VentureAbout.asp>
<http://edr.state.fl.us/Content/returnoninvestment/SSBCIReportFinal.pdf>

¹³¹ Chapter 2009-51, L.O.F.

¹³² <http://www.floridaopportunityfund.com/EnergyAbout.asp>. Also see
https://www.naseo.org/data/sites/1/documents/committees/financing/notes/2011-05-06-Florida_Clean_Energy_Investment_Program.pdf

¹³³ For an overview of how states have used SSBCI funds to supplement, revitalize or create their venture capital programs, see Chapter 4: Observations from Venture Capital Programs, in Cromwell Schmisser (2016, 61-88).

¹³⁴ <http://edr.state.fl.us/Content/returnoninvestment/SSBCIReportFinal.pdf>

¹³⁵ Section 288.95155(1), F.S. Florida Department of Economic Opportunity "2016 Annual Incentives Report," p. 49.
<http://www.floridajobs.org/docs/default-source/reports-and-legislation/final-version-incentives-report.pdf?sfvrsn=4>

¹³⁶ Line Item 1742, ch. 98-442, L.O.F.

¹³⁷ Section 288.95155(3), F.S. The most recent reported investments (FY 2015-16) include: \$350,000 in the portfolio of venVelo, a venture fund and business accelerator focused on early-stage opportunities; \$250,000 in Genicon Investment Group, LLC, a special purpose investment vehicle created by venVelo for the purposes of investing in Genicon, Inc., an emerging leader in the design, production, and distribution of patented surgical instrumentation focused exclusively on laparoscopic surgery; and \$300,000 as a bridge note to Genicon that was later converted into stock in order to leverage an additional \$1.4 million in outside investment. Florida Department of Economic Opportunity "2016 Annual Incentives Report," p. 49.

<http://www.floridajobs.org/docs/default-source/reports-and-legislation/final-version-incentives-report.pdf?sfvrsn=4>

¹³⁸ For an overview of the State Board of Administration, see <http://www.oppaga.state.fl.us/profiles/4040/>.

this state.”¹³⁹ The SBA contracts with an investment company to manage distributions from the state pension fund, which “are stratified among companies that invest in early-stage, growth-stage, and later-stage as well as in debt investments in credit worthy companies.”¹⁴⁰ The Statute limits the fund investments in alternative investments (equity funds, venture capital funds, hedge funds or investments that are not publicly traded) to twenty percent of the fund.¹⁴¹

The Florida Office of Program Policy Analysis & Government Accountability’s (OPPAGA) annual review of the fund reports that, as of June 30, **2016**, the fund “has committed to invest \$512.4 million in 37 technology and growth companies and 29 private equity funds.”¹⁴²

The Florida Institute for Commercialization of Public Research (Institute) assists in the commercialization of products developed by the research and development activities of innovation businesses, publicly supported universities and colleges, research institutes, and other publicly supported organizations within the state. The Institute provides mentoring, marketing information, and access to private investors and venture capital investors.¹⁴³ Through the **Florida Technology Seed Capital Fund**, the Institute also provides \$50,000 - \$300,000 in seed funding to qualified startups, either as debt or equity.¹⁴⁴ The Institute reports that “through the end of FY 2015, the Institute had funded 39 companies across multiple targeted industries...”¹⁴⁵ Since 2007, an estimated \$33 million in state funding has been appropriated to the Institute for operating costs, grants, loans, and seed stage funds.

Florida’s universities are also a source of support for startup businesses, first with the initial funding of research through the academic departments, research centers, institutes, and Centers of Excellence. **University technology transfer offices** obtain patents, copyrights or trademarks, for viable faculty and staff ideas, inventions and innovations.¹⁴⁶ These offices may also provide guidance and support in developing these ideas, inventions and innovations into products or specialized services, and licensing them to a business for development and commercialization.

In lieu of licensing, the faculty or staff may elect to develop and commercialize their product or services through a startup business. Support to these entrepreneurs is provided through university affiliated **business incubators**. Incubators may provide a wide range of assistance, including forming a corporate entity; selecting a management team and developing a business plan; providing office space and shared

¹³⁹ Enacted by ss. 1-4, ch. 2008-31. L.O.F.

¹⁴⁰ “Florida Growth Fund Investments Have Provided Over \$200 Million in Distributions to the FRS; Fund Managers Continue to Seek New Investment Opportunities,” The Florida Office of Program Policy Analysis & Government Accountability, Report No. 16-08, p. 2. <http://www oppaga.state.fl.us/MonitorDocs/Reports/pdf/1608rpt.pdf>

¹⁴¹ See s. 215.47(15), F.S., and s. 215.4401(3)(a)1. & 2. , F.S.

¹⁴² OPPAGA Report No, 16-08, p. 3.

¹⁴³ Ch. 2007-189, L.O.F., s. 288.9625, F.S. <http://www.florida-institute.com/>

¹⁴⁴ Established in 2013 by ch. 2013-120, L.O.F. <http://www.florida-institute.com/programs/company-funding>

This program was preceded by the Institute’s Seed Capital Accelerator Program and the Florida Research Commercialization matching Grant Program.

¹⁴⁵ <http://www.florida-institute.com/news/new-study-unveils-economic-impacts-of-institute-commercialization-of-public-research-0> and <http://edr.state.fl.us/Content/returnoninvestment/SSBCIReportFinal.pdf>

¹⁴⁶ For more detail on these services, see “Technology Commercialization and Startup Primer,” University of Florida Office of Technology Licensing and UF Tech Connect, at <http://research.ufl.edu/otl/wp-content/uploads/STARTUP-PRIMER-2016-Online.pdf>

facilities, equipment, administrative services, and other business support; and marketing the business to investors.¹⁴⁷

Business incubators may also be affiliated with another governmental entity, a not-for-profit or a for-profit organization. There are at least seventy business incubators in Florida – public, private, and a combination thereof.¹⁴⁸ The most prominent incubators are affiliated with state universities, including the University of Florida, the University of Central Florida, and the University of South Florida.¹⁴⁹

Conclusion

This Appendix provides an overview of Florida's financial and technical assistance programs for small businesses; venture capital and state-funded venture capital strategies; and Florida's venture capital programs.

¹⁴⁷ For example, the UF Tech Connect and Innovation Hub offers comprehensive services to startups at the University of Florida. See <http://floridainnovationhub.ufl.edu/about/>, <http://sidmartinbio.org/beta/overview/> and <http://gainesvillebizreport.com/sid-martin-biotechnology-institute-named-worlds-no-1-biotech-incubator/>.

Also see <http://www.fbiaonline.org/> and <http://www.floridatrend.com/article/22175/incubators-help-florida-small-businesses-bloom>

Incubators differ from research and technology parks in their focus on startup and early stage companies. Research and technology parks, on the other hand, tend to be large-scale projects that house everything from corporate, government, or university labs to very small companies. Most research and technology parks do not offer business assistance services, which are the hallmark of a business incubation program. However, many research and technology parks house incubation programs. For a recent overview of university affiliated Research Parks in Florida, see

<http://floridataxwatch.org/resources/pdf/Feb14ECFINAL.pdf>

Incubators differ from business accelerators in that they "accelerate growth of an existing company, while incubators 'incubate' disruptive ideas with the hope of building out a business model and company. So, accelerators focus on scaling a business while incubators are often more focused on innovation."

See <http://www.techrepublic.com/article/accelerators-vs-incubators-what-startups-need-to-know/>

Unlike incubators, accelerators typically limit services to three or 4 month programs.

Also see <http://microventures.com/education/accelerators-vs-incubators> & <http://www.forbes.com/sites/georgedeeb/2014/08/28/is-a-startup-incubator-or-accelerator-right-for-you/>

Startup Accelerators provide short-term mentoring programs that culminate in a public pitch event or demonstration day to potential investors. See Hathaway, Ian. 2016. "Accelerating Growth: Startup Accelerator Programs in the United States."

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¹⁴⁸ Florida Business Incubators Association, <http://www.fbiaonline.org/Incubators/incubators.htm>

Florida Trend, <http://www.floridatrend.com/article/17616/floridas-business-incubators--2015>

¹⁴⁹ <http://floridainnovationhub.ufl.edu/> , <https://incubator.ucf.edu/> & <http://www.research.usf.edu/rf/usf-connect.asp> These three universities have also collaborated through the Florida High Tech Corridor Council (FHTCC) , an economic development initiative, to grow high tech industry in the region through research, research grants, workforce development and marketing programs. See: <http://www.floridahightech.com>

TABLE 2
Funding for Florida Programs Aiding Small and Startup Businesses (\$ in millions)

Program	Capitalization		Six-Year History of Legislative Appropriations					
	Federal	State	12/13	13/14	14/15	15/16	16/17	17/18
<u>Loan & Loan Support for Small Businesses</u>								
Microfinance Guarantee Program	--	--	--	--	10.0*	--	--	--
Microfinance Loan Program	--	--	--	--	10.0*	--	--	--
FL Loan Support Program	47.2	--	--	--	--	--	--	--
FL Capital Access Program	2.0	--	--	--	--	--	--	--
FL First Capital Finance Corp	--	--	--	--	--	--	--	--
Economic Gardening Loan Program	--	10.0**	--	--	--	--	--	--
<u>Technical Assistance for Small Business</u>								
Economic Gardening Tech Assistance	--	10.0**	2.0	1.0 vetoed	--	--	--	--
FL Small Business Develop Center Network	--	0.5	--	4.0	--	--	--	--
<u>Venture Capital</u>								
FL Opportunity Fund	--	28.0	--	--	--	--	--	--
Clean Energy Investment Program		36.1						--
FL Venture Capital Program	43.5	--	--	--	--	--	--	--
FL Small Business Tech Growth Fund	1.5	--	--	--	--	--	--	--
Florida Growth Fund of the SBA		***						--
Inst for Commercialization of Public Research	0.9	10.0	1.0	5.5	5.5	5.5	5.5	--

* \$10m was appropriated for both the Loan and Guarantee programs, the allocation of which was unspecified.

** \$10m was appropriated for both the Loan and Technical Assistance programs, the allocation of which was unspecified.

*** Up to 20% of an estimated \$2.1 billion is authorized to be distributed for investments in alternative investments.

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