

Department of Legislative Services
Maryland General Assembly
2004 Session

FISCAL AND POLICY NOTE
Revised

House Bill 905 (Chairman, Environmental Matters Committee, *et al.*)
(By Request – Departmental – Housing and Community Development)

Environmental Matters

Education, Health, and Environmental Affairs

**Department of Housing and Community Development - Neighborhood Business
Development Program**

This departmental bill authorizes the Department of Housing and Community Development (DHCD) to provide financial assistance to microenterprises under the Neighborhood Business Development (NBD) program. It also expands the source of funds for NBD programs to include Community Development Administration (CDA) revenues.

Fiscal Summary

State Effect: Program loans for microenterprises would be supported by \$1 million anticipated revenue from the sale of loans in DHCD's portfolio each year. Although any such sale of loans would increase special fund revenues in the short term, special fund revenues could decrease over the long term to the extent that the bill allows DHCD to sell up to \$4 million of loans or loan proceeds at a discount. The decrease would likely be minimal. General fund revenues could increase to the extent that additional loans authorized by the bill spur job creation and sales tax activity. To the extent that eligibility for CDA funds is expanded, those funds could be diminished more rapidly.

Local Effect: Local government revenues would increase to the extent that the additional business activity resulting from the bill provides additional income tax revenue. Under one scenario, local income tax revenue would increase by \$190,400 after three years.

Small Business Effect: DHCD has determined that this bill has a meaningful impact on small business (attached). Legislative Services concurs with this assessment. (The attached assessment does not reflect amendments to the bill.)

Analysis

Bill Summary: A microenterprise is a business with five or fewer employees that requires no more than \$35,000 in start-up capital and does not have access to traditional commercial banking. The bill specifies that microenterprises and nonprofit organizations are eligible for financial assistance under NBD and that the need to finance microenterprises or nonprofits (in addition to small businesses) to upgrade a neighborhood may be considered a factor in the designation of a qualifying neighborhood.

The bill also authorizes DHCD to sell, assign, or otherwise dispose of any NBD loan or loan proceeds. These loans can be sold at a discount. However, the maximum sale proceeds in any fiscal year cannot exceed \$4 million, and the sale proceeds must be applied to the NBD Fund. DHCD must make a reasonable good faith effort to commit 25% of NBD loans and grants to microenterprises.

The bill directs CDA to make money available for NBD programs but does not specify an amount. DHCD may transfer unencumbered funds from NBD to certain housing funds (including Rental Housing and Homeownership), subject to State laws and the approval of the Legislative Policy Committee.

Current Law: NBD was created in 1995 to stimulate investment in Maryland's older communities by developing, redeveloping, or expanding small businesses, investing in revitalizing small businesses, and helping local governments develop and expand small businesses. It provides below-market interest rate loans to small businesses and small nonprofit organizations locating or expanding in locally designated neighborhood revitalization areas. Financing ranges from \$25,000 to \$500,000 for up to 50% of a project's total cost. Retail, manufacturing, and service-related businesses are eligible, as are mixed-use projects that contain commercial or retail use at street level and no more than 12 residential units.

CDA is charged with increasing housing opportunities for families of limited income, the elderly, and the disabled. Programs that increase home ownership, improve rental housing, build group homes, and assist owners with rehabilitated housing are overseen by CDA. Programs are financed by the sale of tax-exempt and taxable bonds, general obligation bonds, special funds, and other sources. The bill allows unencumbered NBD funds to be transferred to any other programs under Neighborhood Revitalization besides NBD, including Community Legacy and removes DHCD's authority to transfer funds from NBD to certain housing funds.

Background: The Aspen Institute and Association for Enterprise Opportunity have identified 650 nonprofit microenterprise programs in the U.S., including some that have

State or federal government partnerships. According to the National Conference of State Legislatures, the District of Columbia has the highest number of programs per capita, followed by Vermont, Maine, Nebraska, Alaska, and Montana. Montana and Nebraska have intermediary organizations that assist and advocate for these programs. The Montana program supports microenterprises by leveraging funds, mobilizing loan capital, and providing staff training and program networking.

There are approximately 2 million microentrepreneurs in the U.S., a majority of whom are women with children. Common industries for microenterprises include jewelry making, furniture repair, computer technology, and personal care services such as hair braiding. A 1999 study by the Aspen Institute revealed that 78% of microentrepreneurs experienced household income gains over five years; the gains were sufficient to allow 53% of them to move out of poverty.

State Fiscal Effect: DHCD advises that it has 138 loans in the NBD portfolio with an outstanding balance of \$22 million as of June 30, 2003; the estimated fiscal 2005 repayment revenue is \$4 million. Up to \$4 million of these loans would be sold or assigned each year under the bill, of which 25% would be used to support microenterprise development. The remaining \$3 million would finance other small businesses through current programs.

DHCD advises that loans would likely be assigned to a nonprofit aggregator called Neighborhood Investment Fund, which would receive the payments from a borrower in exchange for an upfront payment to DHCD. The department advises that the sale or assignment would be based on the demand for future loans, which would be offered at an identical interest rate (4%) as the loans that are assigned. Any sale of loans (or transfer of payment rights) would have to be approved by the Board of Public Works. The Department of Legislative Services advises that special fund revenue loss would be incurred in subsequent years if the loans were sold at a discount or the borrowers defaulted. The program has had a consistently low default rate of 5% so any such revenue loss is not expected to be significant.

DHCD advises that the microenterprise loans could generate an annual payroll of \$12.4 million after three years, thus increasing State sales and income tax revenue (combined) by \$535,572.

DHCD has never transferred funds from NBD to another program despite its current statutory authority to do so. The bill's proposal to allow transfers from NBD to other programs within the same division could affect the availability of NBD funds to the extent that they are transferred.

Small Business Effect: DHCD estimates that 67% of small businesses fit the definition of a microenterprise. It expects that the average loan under the proposed program would be \$17,500 and support 55 new projects per year, based on \$1 million from the sale or assignments of loans authorized by the bill each year. Each loan is assumed to result in the hiring of three new jobs, for a total of 513 new jobs over three years.

Small businesses that qualify for other NBD loans would also benefit from the \$3 million anticipated from the sale or assignment of loans that would be used to finance additional loans or guarantees.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Department of Housing and Community Development, National Conference of State Legislatures, Department of Legislative Services

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