Sustainable Funding for Early Stage Small Businesses in the State of Ingenuity:

An Analysis of Business Readiness for Capitalization

A Report to the

United States Economic Development Agency

Brian Richard
Joey Lata
Jennifer Groce
Norman Walzer
Brian Harger
Andy Blanke

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Executive Summary

This report is intended to help local development practitioners and public officials gain insight into new and innovative approaches to helping entrepreneurs finance business starts. Focused geographically on six counties in northern Illinois and southern Wisconsin that were hard hit by flooding and the Great Recession, a region designated as the State of Ingenuity, the report findings are relevant to other regions in the U.S. that wish to strengthen the connection between entrepreneurs and startup capital or early growth funding. Key findings are summarized below.

- While the SOI region is mostly rural, it has shown promise in terms of business startups. Each of the six counties in the region had business startup rates higher than the Wisconsin/Illinois average in the four-year period immediately prior to the recession. However, this is offset by higher business closure rates in the same period.

- A majority of business startup financing comes from personal savings, personal credit (home equity, credit cards), and/or friends and family. Debt financing is the next most common source for startup capital. According to national studies, bank loans are the most common type of debt financing.

- Technical assistance regarding financial planning is important to the success of some small businesses. Many entrepreneurs have expertise in their business sector but may not understand how to compile, analyze, and/or project financial statements and are refused traditional bank financing despite the potential for successful expansion.

- Successful small business financing programs combine capital sources with financial counseling to coach the entrepreneur through the process. Some small banks provide this through relationship lending. For the most part, national banks are more focused on loan volume and don't spend enough time with small business owners to educate potential borrowers about what is important for a loan.

- Financial resources for small business in the SOI region are available at the regional, state, and federal levels. Regional resources include revolving loan funds and an angel investors group. Both Illinois and Wisconsin have finance programs for small business, primarily aimed at historically underserved populations or types of businesses. Federal programs include the US Department of Agriculture’s Business and Industry Guaranteed Loan Program and the Small Business Administration 7a and 504 programs.
Effective practices from other regions may be adapted and implemented in the SOI region. Examples include:

- **Network Kansas** provides a resource clearinghouse to help business managers find appropriate resources.
- **Capital through Counseling** uses a capital coach to help small- and medium-sized enterprises find financing.
- The **Plato Initiative** forms small groups (about 10-20 members) of mainly small business managers who meet to learn management skills from their peers and gain business and personal connections that lead to commercial opportunities.
- **Economic Gardening** that fosters economic development providing entrepreneurs with technical assistance in the form of research on their markets, competitors, and industry trends.
- The **Kentucky Highlands Investment Corporation (KHIC)** offers financing, entrepreneurial training and managerial assistance and coordinates activities of service providers across the region.

These findings suggest recommendations in four areas: research, training, capital sources, and regional coordination.

**Research: Small Business Financing Experience:**

**Need:** The majority of research on small business lending focuses on the source and amount of financing for which small businesses apply and do not deepen understanding of the financing experiences, decisions, and detailed needs of specific entrepreneurs.

**Recommendation:** *Initiate a research effort focused on the financing experiences of small businesses that could be helpful in designing better products and services to help entrepreneurs grow or expand their businesses.*

**Research: Angel Investor Identification**

**Need:** Angel investors are “wealthy individuals, typically fellow entrepreneurs, willing to invest in the very early stages of a venture development” (Morrissette, 2007, p. 52).

Angels typically invest in industries they know and many are hands-on investors who meet frequently with the entrepreneurs they finance. Consequently, over 75% of angel investors
invest in companies within 50 miles of their residence. There are several angel investment networks in the region. Local business development experts believe that there are many other potential angel investors in the region.

**Recommendation:** Launch a systematic effort to identify angel investors in the SOI region. A snowball sampling technique would broaden the reach beyond the original set of interviewees.¹ The survey findings could be shared on a website or other media with potential entrepreneurs. In addition, discussions with the angel investors regarding interests in specific business ventures could help development practitioners identify potential entrepreneurs. Angel investors could also help by indicating the types of information they find most useful and the formats they prefer. All of this information could be shared through informational and training efforts for entrepreneurs as discussed in the next recommendation.

**Training and Technical Assistance**

Need: Many early stage entrepreneurs lack the financial skills and knowledge to obtain financing. Many do not even approach banks, assuming they will be denied funding. As such, potentially successful businesses are underfunded.

**Recommendation:** Provide small businesses with access to more sophisticated market analyses, assistance with financial calculations and projections, and information about federal, state and local financing programs. Offer information to financial service providers about opportunities to provide financing to entrepreneurs and about strengthening coordination of financial services ranging from face-to-face counseling to internet or phone-based services.

¹Snowball sampling employs a question at the end of each interview asking the participant to identify others who might have information related to the study.
**Small Loan Sources**

Need: Small businesses have a special need for loans of less than $50,000. Banks are hesitant to make small loans because of the high administrative costs relative to the revenue generated.

There are few sources of small loans. Accion Chicago makes loans (up to $20,000 for startups and $50,000 for expansions) and they recently expanded their territory to include the Rockford region but do not make loans in Wisconsin. Local RLFs are often willing to loan smaller amounts but may be more difficult to find.

**Recommendation:** Improve access to capital by more fully utilizing existing resources and attracting new resources to the region. Revolving loan funds are underutilized, especially in the more rural parts of the region. Improved communications among lending agencies could lead to collaborative projects and/or could reduce the transaction costs for small borrowers. Likewise, coordinated efforts in the region to bring in new lending agencies such as Accion could lead to additional financing opportunities for startups and/or expansions.

**Regional Partnerships and Coordination**

Need: Despite the lack of a regional umbrella organization, informal regional collaboration is happening. Entrepreneurial support programs such as the GrowthWheel, started at EIGERLab, are spreading to organizations across the SOI region. GrowthWheel brings the service providers together to identify solutions to help the entrepreneur achieve success with short-term goals. EIGERLab also pioneered the FastPitch entrepreneurial competition in the region, hosting the first competition in 2007. In 2012, both UW-Parkside in Kenosha and the UW-Whitewater Innovation Center started competitions.
Recommendation: Build on the early successes of such regional programs such as FastPitch and GrowthWheel. These programs spread through the region through informal interaction. A regional policy network would facilitate this type of regional learning. A policy network brings together entrepreneurs, government officials, policymakers and others who are interested in developing effective entrepreneurship policy. An effective policy network includes an organization that is responsible for collecting and disseminating regional activities and events as well as keeping up with the latest successful practices from other regions.

Especially important is that the region work as a unit. This is critical for the small agencies in less densely populated areas. To succeed, they will have to build on the efforts of the larger cities and regional centers. Linking the financial centers with development agencies that work with small businesses will be key to a prosperous future. This coordination will be much more successful if there is a lead umbrella organization to provide leadership and assume responsibility for outcomes.

Path Forward

These four areas (research, training, capital sources, and regional coordination) are interrelated. Training Revolving Loan Fund managers will help businesses access available funds. By expanding on the informal regional coordination currently underway, experienced RLF managers can mentor newer, less experienced managers. The research outlined can help better design training programs that help current entrepreneurs more effectively tap into existing traditional finance sources as well as guide policymakers toward effective programs underway in other areas.
Introduction

The State of Ingenuity region including six counties in Illinois and Wisconsin has suffered from both national disasters such as flooding and from serious economic setbacks in the Great Recession that closed one automobile factory and caused serious cutbacks in another. While some employment has returned, it is important that efforts continue to revitalize and transform the economic base for long-term prosperity. Local economic development practitioners recognize the importance of business starts and expansions to regional prosperity.

Obtaining adequate financing for business starts and expansions is at the heart of local economic development. The SOI region is no different from most other areas in encountering difficulties in financing business starts. Banks and financial institutions, because of tighter regulations and the lack of collateral available to borrowers with declines in housing values, have been less willing to finance new businesses.

The current project examines access to traditional financing opportunities—both debt and equity. Information about bank lending is provided along with a review of equity options in the region. Attention then turns to innovative practices in other states that have tried to increase access to capital using a variety of initiatives, some of which have potential for the SOI region, although Illinois and Wisconsin differ in legislation and requirements regarding lending practices.

The intent of this report is to help local development practitioners and public officials gain insight into new and innovative approaches that could be tried in the SOI counties, as well as in other regions across the United States, to help entrepreneurs finance business starts. While the experiences with business starts in the region have been comparable or
better than other semi-rural areas, additional effort and new options will be needed to help start-up businesses survive and grow during the recovery. Several programs that may be tried in the SOI region are described in detail in this report.

Background

The past decade has brought economic setbacks to many regions metro and rural alike. The shift from a relatively prosperous 2000s to the Great Recession starting in 2008 wreaked economic havoc causing double-digit unemployment and business closures with ripple effects throughout the regional economy. In this environment, local economic development agencies struggled daily to find ways to retain, attract, and start businesses to replace those that closed due to retirements or economic shifts. Markets, technological advancements in production processes, and the availability of labor or other inputs are all important considerations affecting business starts or expansions. Underlying all of the factors is access to capital, without which businesses cannot start or expand.

Numerous regional development strategies are employed by local development agencies depending on size, geography, demographics, industrial composition, and other considerations. Business creation and expansions leading to additional job creation are key components in most, if not all, regional strategies. Since the 1960s, it has been well-understood that more employment is generated by small businesses, variously defined, than by large companies many of whom have downsized during productivity improvement approaches (Birch, 1987; Baily et al., 1994). Thus, current job creation and economic development initiatives emphasize small business development and the launch of startup companies (Creating the Next Regional Frontier, 2009).
A large literature exists on factors associated with entrepreneurs and their efforts to launch businesses. Especially important are: an entrepreneur's commitment and willingness to take risk, ingenuity, industry affiliation, market demand, business model, operating environment, access to necessary resources, and appropriate support mechanisms. There also is clear evidence that population characteristics are associated with business starts including several cohorts such as young females, Hispanics, pre-retirees, farmers with small acreages, and unemployed (Walzer and Blanke, 2013). According to these attributes, there is clear evidence of an active entrepreneurship climate across the region.

The State of Ingenuity (SOI) project, with funding from the United States Department of Commerce, Economic Development Administration, organized economic development stakeholders in a six-county region including northern Illinois (Boone and Winnebago counties) and southern Wisconsin (Kenosha, Racine, Rock, and Walworth counties) into an effort to provide services in a more coordinated fashion. All except Walworth County are in Metropolitan Statistical Areas and Walworth is a micropolitan county. (US Census, 2009).

The project involves collaboration among 12 entities to support entrepreneurial approaches. The SOI partnership is a network of universities and colleges, economic development agencies, and business incubators with a goal to deliver services in ways that promote new businesses in the region, grow and expand existing businesses, and increase

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2A metro area contains a core urban area of 50,000 or more population, and a micro area contains an urban core of at least 10,000 (but less than 50,000) population. Each metro or micro area consists of one or more counties and includes the counties containing the core urban area, as well as any adjacent counties that have a high degree of social and economic integration (as measured by commuting to work) with the urban core.
private investment. The ultimate outcome of these efforts is to create jobs and wealth in the region.

Key to entrepreneurial efforts and sustainability is access to financing, an issue critical to the efforts of all SOI partners. Consequently, as one of several key activities in the overall SOI effort, the Center for Governmental Studies at Northern Illinois University conducted research on access to finance in the region as well as innovative practices that have worked in other regions across the United States.

The findings in this report provide SOI participants and other economic and business development professionals with more insight into the small business financing landscape that, in turn, can help them access more capital in the region. The focus throughout this project is on small businesses: establishments with fewer than 50 employees. As will be shown later, these businesses represent a substantial proportion of the ventures in SOI counties and are critical to economic prosperity.

This report has several parts. First, the typical business development life cycle is described, along with common sources of funding used at each stage of growth. The second main section describes financing sources currently available for businesses in the SOI region. The third section focuses on promising practices in other regions that could yield results in the SOI region. The final section discusses possible options for the SOI region based on successful practices.

**Background Profile**

There has been considerable research on characteristics of entrepreneurs. Entrepreneurial intention and action are prevalent in all demographic groups. Appendix A
provides a profile of entrepreneurs and compares that profile to the demographics of the SOI region.

Small companies, especially those in early stages of development, have traditionally encountered obstacles to obtaining capital (Markley, 2007). Banks and other traditional financing entities have difficulties making a profit on small loans because of high information costs (i.e., checking on credit worthiness, etc.) relative to the expected return.

Entrepreneurs have difficulty communicating the appropriate information that loan officers are seeking (e.g., business plans, historical and pro forma financial statements, etc.). This is especially true in rural areas with fewer lending institutions and fewer entrepreneurs. More recently, with restrictive regulations, risk avoidance following the major housing losses during the housing finance crisis, and consolidation of banking activities with development loan decisions now made at more distant locations, entrepreneurs have even more difficulty obtaining capital (Federal Reserve Bank of New York, 2012).

**Business Development**

Various models depicting life cycle stages of a business exist, with some focused on specific types of businesses, such as the technology or service industries. The differences among the models sometimes are relatively minor and based on *growth* patterns. Growth is an increase in scale without changing business structure. Life cycle models often concentrate on a specific dimension of the business, such as management or marketing. Stages in many models are often really business strategies such as stability, harvesting, or diversification.
More useful in the current project are the life cycle stages in a business that focus on development patterns. Business development is a process that occurs over time with different requirements and operations in each stage. Effectively working with businesses requires that the stage of business is accurately assessed so that the needs and issues facing the business can be targeted based on change strategies that will move it to the next higher stage of development.

Types of assistance needed differ at each development stage of the business. An important component sometimes missed when assisting in business development is the skill level and experience of the entrepreneur. The success of business development support requires awareness of both these aspects (Lichtenstein & Lyons, 2010). A business idea conceived by an entrepreneur with no previous experience requires extensive education, services, and support. An experienced entrepreneur who has already achieved success in developing a business may require less education and support.

Entrepreneurs engaged in new business development at the earliest stages of the life cycle have access to a variety of programs such as accelerators, incubators, government-sponsored business development centers, and university research/entrepreneur programs. Assistance with access to capital is among the top services provided by business development programs. In a study for the US Department of Commerce, Economic Development Administration, startups reported access to capital as the underlying cause for their failures (Baily, Dynan, and Douglas, 2010).
Life Cycle Stages in Business Development

Learning how life cycle stages influence entrepreneurs, what their firm’s specific needs are, and the help offered by coaches, consultants, and advisors are important in designing an actionable, universal model for stages in the business life cycle. Lichtenstein and Lyons (2010) studied 26 different life cycle models. Their approach, the basis for describing business development activity in this report, includes:

- **Stage 0: Pre-Venture:** Desire to start or own a business on the part of an entrepreneur, making a commitment, determining feasibility, developing the offering, assembling the team. The key focus for this stage is formally developing the business concept. Preparing a business plan is essential. Early formal planning by the entrepreneur results in a steady pace of start-up activities, leading to increased success at getting into business (Liao & Gartner, 2009)

- **Stage 1: Existence or infancy:** Product or service is ready for sale and a small set of customers show interest. This stage ends by breaking even from sales.

- **Stage 2: Early growth:** A critical mass of customers is satisfied and sufficient cash flow is available for asset replacement or repair. As long as market conditions remain, the stage ends with an established, sustainable business.

- **Stage 3: Expansion or sustained growth:** Healthy profits and growth potential allow borrowing or equity to finance growth. The company has proven capability to serve customers, delivers a variety of products/services, captures market share, and withstands competitors. The business is of sufficient size and earns a substantial return on labor and assets.

- **Stage 4: Maturity:** Established in size and stable, the business has a strong market position, is profitable, has positive cash flow, and a strong management team with an effective system of controls. Market saturation and competition are inevitable. Protection of existing assets while searching for new market opportunities will require careful balance.

- **Stage 5: Decline:** Market share begins to decline due to complacency or risk-aversion.
Figure 1: Stages of Business Development

Source: Lichtenstein and Lyons, 2010, p. 70

The State of Ingenuity initiative focuses on increasing the success and capital needs of small business starts in pre-venture businesses about to launch (Stage 0), those in infancy that have started and are striving to achieve profits (Stage 1), and early growth and expanding businesses (Stage 2). Various financing options are available for business development, often based on the business life cycle stage (Table 1. Also see Appendix B for definitions).

Sources of Startup Financing

Debt and equity capital sources offer different levels of support in all stages of business development. Finding ways to encourage businesses to grow and expand with capital beyond the entrepreneur’s personal resources is central to development initiatives. Descriptions of capital funding choices available to small businesses vary based on the data source, but it is clear that two sources stand out in importance for financing small business: the owner’s personal funds and bank loans. Appendix C contains a detailed discussion of small business financing options.
As described previously, businesses finance growth through a combination of equity and debt. This section describes these sources in more detail. Challenges in using these sources are also explored.

Table 1: Sources of Business Financing

<table>
<thead>
<tr>
<th>Business Life Cycle Stage</th>
<th>Finance Type</th>
<th>Source</th>
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<tbody>
<tr>
<td>Zero</td>
<td>Debt or Equity</td>
<td>Friends and Family</td>
</tr>
<tr>
<td>Zero - One</td>
<td>Debt</td>
<td>Microfinancing</td>
</tr>
<tr>
<td>One</td>
<td>Debt</td>
<td>Customer Financing</td>
</tr>
<tr>
<td>One</td>
<td>Debt</td>
<td>Community Supported Enterprises</td>
</tr>
<tr>
<td>One or Two</td>
<td>Debt</td>
<td>Vendor Financing</td>
</tr>
<tr>
<td>One or Two</td>
<td>Debt</td>
<td>Convertible Debt</td>
</tr>
<tr>
<td>One or Two</td>
<td>Debt</td>
<td>Capital Equipment Loans and Leases</td>
</tr>
<tr>
<td>One or Two</td>
<td>Debt</td>
<td>Working Capital Financing</td>
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<td>Two or Three</td>
<td>Debt</td>
<td>Venture Debt</td>
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<tr>
<td>Two or Three</td>
<td>Debt</td>
<td>Bridge Loans</td>
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<tr>
<td>Zero - One</td>
<td>Equity</td>
<td>Crowdfunding</td>
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<td>One</td>
<td>Equity</td>
<td>Accelerator Programs / Contests / Prizes</td>
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<td>Equity</td>
<td>Community Supported Enterprises</td>
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<td>One or Two</td>
<td>Equity</td>
<td>Mergers and Acquisitions</td>
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<tr>
<td>One &amp; beyond</td>
<td>Equity</td>
<td>Strategic Partnering</td>
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<td>Three &amp; beyond</td>
<td>Equity</td>
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<td>Neither</td>
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</tr>
<tr>
<td>One or Two</td>
<td>Revenue share</td>
<td>Revenue-based Financing</td>
</tr>
</tbody>
</table>

**Debt Financing**

Debt financing is an important source of capital for a developing and early stage business (Walker, 1989; Bates, 1997; Berger and Udell, 2002; Cassar, 2002; Chua et al., 2009). This type of financing refers to money borrowed that requires repayment, usually with interest rates that vary widely by source. Rates are influenced by factors such as the owner’s personal credit, assets associated with the business, and amount of capital sought.
Debt financing is especially appealing because it allows a business owner to maintain full control at a lower cost (Walker, 1989; Walter, 2004). Small firms rely on a variety of debt sources including bank loans, loans from friends and family, personal home equity loans, personal credit cards, trade credit, and other informal sources of financing (Ang, 1992; Peterson and Rajan, 1994; Ang, Lin, and Tyler, 1995; Berger and Udell, 1995; Binks and Ennew, 1996; Cole and Wolken, 1996; Berger and Udell, 1998).

The Kauffman Firm Survey annually tracks a group of businesses founded in 2004. Among the findings of these analyses was that external debt was the largest source of funding in the first year of operation (Robb, et al., 2010). On average, new firms borrowed $80,000, of which $32,000 was debt from bank loans, credit cards, and similar sources.

Several types of debt financing are available to startups. Small business ventures can access four main sources of debt finance during their developing and early stages: *personal financing*, including friends and family; *bank financing*, including credit cards, lines of credit and loans; *trade credit*; and *government/non-institutional* financing. The nuances in each type of debt can influence the way businesses start and grow. Some of these differences are described next with more details about various forms of debt financing in Appendix D. 

Personal investment is the most used source of capital in the initial development phase. The Small Business Administration (SBA) reported that personal savings was the number one source of start-up capital for small businesses in Stage 0 and, on average, 60% of small business firms seeking start-up capital use a combination of personal and family savings (SBA, 2011). Personal savings and resources such as credit lines that borrow against personal assets allow an owner to maintain the most control of the business (Lopez-Garcia and Aybar-Arias, 2000; Blumber and Wilko, 2008). Even when financing from personal
funds is structured as a loan, financial institutions frequently view it as equity because the owner loans are subordinate to other types of financing.

Investment from friends and family with an established repayment plan is considered debt, as compared to an equity position with the company, sharing profits from the firm. Friends and family may provide a relatively easy way to access loans and usually is in addition to personal investment (Walter, 2004). Firms with a lack of tangible assets (i.e., no asset structure) tend to rely on capital from less formal means such as friends and family (Cassar, 2002).

As their businesses grow, entrepreneurs often have financing needs beyond what friends and family or credit cards can provide. At this point, they typically seek bank loans to finance growth. Business owners should provide credible commitments and signals to the bank to increase confidence that the business is likely to succeed and be able to repay the loan even if it fails (Avery, et al., 1998; Blumberg and Wilko, 2008). Banks evaluate this through the ‘three Cs’: character, credit, and collateral. Smaller local banks are often in a better position to evaluate character while larger national banks place greater emphasis on credit scoring.

Community banks are institutions with less than $1 billion in total assets. “Small businesses consistently appear more willing to ask for credit when their bank is a regional or community bank (and they appear to be more successful in their requests)” (Dennis, 2012). Community or small banks’ greater reliance on relationship lending can help address some issues associated with lack of clear information, which may lead to higher rates of lending. According to Berger and Udell (2002), “a small bank may be able to resolve some contracting problems associated with the relationship lending by eliminating layers
of management and reducing the agency problems between the loan officer and senior management”.

The Small Business Administration (SBA) provides access to loan enhancement programs to banks, credit unions, community development financial institutions (CDFI’s), and community development corporations (CDCs). The SBA 7a and 504 loan enhancement programs are available to banks to help reduce the risks that may otherwise prohibit them from lending to small firms in their early stages.

Additional sources of debt financing are available from several government assisted and/or not-for-profit financial entities that provide diverse low interest loan programs to meet a diversity of small business start-up needs. National, state, and even local program focus on encouraging small business growth. These programs often involve low interest loans backed by federal programs or grants. Community Development Financial Institutions (CDFI) and revolving loan funds (RLF) are two common tools used at the municipal or county level to support business development directly. Both government and non-governmental organizations provide minority groups or target industries such as technology innovation with designated funding in response to identified needs in the region.

Microfinance agencies provide financial services to populations, such as those in poverty, without access to typical banking services (Hoje et al., 2009). Started as a movement towards social responsibility to eliminate poverty in developing countries, microloan programs have been adapted in the United States and enable individuals to start businesses without access to traditional bank capital. Microloans in small amounts are made at high interest rates for a short term (Hoje et al., 2009). Most of the entrepreneurs
receiving microloans will not become large employers in the region but, nevertheless, can employ several workers which is important in small rural economies.

**Challenges in Debt Financing**

Many challenges face debt-based capitalization of new and early stage firms. These challenges include a lack of information, limited access to long-term credit, and risks associated with liabilities associated with newness of the business (Stichcombe, 1965; Chau et al., 2009). The imbalances caused by newness and risk have significant impacts. Small firms have access only to segments of the traditional debt finance markets that are limited by entry barriers and the size and capital needs of a small firm (Walker, 1989). Debt financing for early stage and new small businesses is difficult from the start due to the limited availability of financial information (opaqueness). Opaqueness is more prevalent in the initial stage of a small business start and is a barrier for traditional finance (Berger and Udell, 1998; Cassar, 2002). The limited information for new ventures can lead to less capital available at higher rates and consequently can discourage use of bank finance (Chua et al., 2009; Cassar, 2002).

In addition to the limited information and risks associated with inexperience, small businesses in the development stage must contend with challenges typically unseen by credit seekers. From a banker’s perspective, the lack of detailed knowledge about industries and/or other small business operations represent an ‘agency problem’. The agency problem arises when the borrower takes control of the lender's asset through a loan. Borrowers may use the asset in their own best interest, which may not always be in the best interest of the bank. These issues, plus the high administration costs relative to
loan size, are significant challenges inherent with debt financing by banks that successful borrowers must overcome.

Agency problems are directly associated with limited access to bank capital. “Consequently, as predicted by agency theory and observed in practice, lenders manage risk by credit rationing through the accept/reject decision and the amount of loan approved” (Chua et al., 473). Small banks and their greater reliance on relationship lending can help to overcome the agency problem in small business lending. “Relationship lending represents the informational privilege that a bank accumulates over time by establishing close ties with its borrower” (Ongena and Smith, Giannetti, 2012, 763).

Small banks have fewer managerial layers and a more direct relationship between the manager and loan officer. This results in a better understanding and appreciation of “soft” information (Berger and Udell, 2002). Studies have found that entrepreneurs have greater success overcoming these problems by working with small community banks and increasing their social capital, which includes incorporating the social capital of friends and family (Chua et al., 2009). However, research based on responses to the SOI bank survey (Richard, Walzer, and Blanke, 2013) indicates that this may not be the case in recent years since the authors found a negative relationship between bank size and small business loan growth.

Discussions about the cost of credit with borrowers most often covers interest rate terms for debt financing, but the cost of credit from a lender perspective requires additional considerations. The smaller the amount borrowed, the less profitable an institution is in terms of interest/revenue generated. Costs associated with gathering information about the small business are high relative to the gains from small transactions
Blumberg and Letterie, 2008), so the benefits often do not outweigh the costs for small loan amounts. Community Development Financial Institutions (CDFIs) and Community Development Corporations (CDCs) can face similar conditions.

Lack of assets is also a cause of concern for financing institutions and represents a roadblock to recouping investment if entrepreneurs default on payments. Bank financing for small firms depends mainly on the ability to secure debt with tangible assets because of limited information about the firm, lack of alternative risk reducing factors, and prevalent use of relationship financing (Storey, 1994; Berger and Udell, 1998; Cassar, 2003). Firms lacking tangible assets tend to obtain capital from less formal means such as friends and family (Cassar, 2002).

The problems associated with a lack of assets can be mitigated by a firm’s expressed intent, ability, and progress towards growth. Firms that plan to grow are more likely to use bank credit. Establishing a credit relationship with financers early on positively influences access to credit and cost (Cassar, 2002).

While access to bank debt is limited in the early stages of a business, accumulating too much personal or non-traditional debt can also negatively affect the ability to access long-term institutional debt financing. Entrepreneurs use higher-cost credit cards as an alternative to addressing issues faced in obtaining small loans. Credit cards with higher interest rates offer quick cash injections that may seem less expensive than equity injections but may hinder continued operations or growth in the long run.
Economic Conditions

Credit supply and consumer demand are additional challenges to financing new and early stage businesses. According to the Federal Reserve's flow of funds account, household net worth peaked in 2007, but fell approximately 28% during the next two years (Board of Governors of the Federal Reserve System, 2013). The loss of income and lower value of personal property brought cautionary spending patterns resulting in a decrease in consumer demand. This decrease in demand led to lower business profits and growth, as well as fewer opportunities for expansion. According to the National Federation of Independent Business (NFIB):

The small business problem has been and remains weak sales; the secondary small business problem is and remains housing in specific and real estate in general. The incapacity and/or reluctance of small business owners to access the credit system are the result of both.” (Dennis, 2011).

An FDIC panel (January 2011) concurred with the NFIB’s findings. During his testimony to this panel, Federal Reserve Board Chairman Ben Bernanke discussed the concept of a “virtuous circle” regarding the relationships between impacts of the recession on sales, consumer demand, credit worthiness, and eventually demand for capital by small businesses.

If the sales come, that will make these businesses stronger, make them more creditworthy and it will be a virtuous circle... More cash flow and also higher collateral values makes businesses more creditworthy, gives them more credit demand, allows them to expand, allows them to hire.
According to Bernanke, as the recovery grows in strength, small businesses will become stronger and be better able to obtain financing for expansions in the future. A weak recovery is likely to continue the current difficulties in obtaining finance.

Since Bernanke’s speech at the FDIC event, access to loans has in fact improved. National survey data from NFIB shows that loan availability for small business has steadily recovered (Figure 2). In March 2013, the index reached its highest point since 2006.

Figure 2: Availability of Loans: Net Percent (“Easier” Minus “Harder”) Compared to Three Months Ago (Regular Borrowers).

While limited information and risks associated with new ventures are especially important in early stage debt financing, entrepreneurs can sometimes overcome these
challenges. Nevertheless, debt remains one of the most affordable, easiest, and accessible sources of capital for new and early stage businesses.

**Opportunities in Debt Finance**

Financing new and early stage businesses with debt capital offers entrepreneurs greater control of the business than relying on equity capital and there are ways to minimize the challenges associated with financing business starts and expansion using debt. Serious planning, including conscious management of debt, social capital, and assets, can bring more success in seeking longer-term debt especially from small banks. Use of personal funds and financing from related sources is essential in establishing commitment. Use of public financing resources and other institutional financing opportunities, such as local revolving loan funds, state grants, and specialized funds from CDFIs and CDCs, are often overlooked, but public financing sources often offer additional opportunities to raise capital. Again, the issue may be more that small business owners are not aware of the programs or think that they would be refused for a loan.

**Equity Financing**

Financing a startup using equity involves investing money for ownership in the business. This approach does not require loan repayment and provides higher credibility for the business, especially when the investment comes from high profile investors who intend to recover their investment through future profits. Founders of new businesses, but not necessarily small businesses, seek equity financing because it involves fewer regulations and the transaction costs of submitting their business plan to investors is relatively small. Experts recommend equity sources of capital for some small businesses due to limitations on the amount of capital available through debt financing alone (Wu et al., 2006).
A disadvantage comes from dilution of ownership, costing the founder loss of autonomy and control. Investors are partners and expect to have a say in business decisions. Small businesses seldom use equity finance for fear of losing control over their companies (Mishra & McConaughy, 1999) and because of unwillingness to comply with increased transparency requirements concerning business transactions (Wu et al., 2006). Small businesses, especially family-owned establishments, may sacrifice expansion opportunities to retain personal control of their companies.

High growth firms are the most likely to receive external equity financing. Traditional external investors expect sales of at least $10 million within six years of starting before considering financing a business. Only 4% of businesses expect to achieve that level of sales in the first six years (Shane, 2009).

Founders must understand the fit between their business and an investor before pursuing equity finance (Shane, 2009). One issue with entrepreneurs involves having the time and expertise to create a business plan sufficient to justify a large investment. Traditional sources for equity financing include individual investors (angels) and institutional investors (venture capitalists). For details about various forms of equity financing, see Appendix E.

**Strategies for Establishing and Sustaining Adequate Capital**

The previous section described funding sources available to entrepreneurs. This section describes mechanisms by which these types of funding are facilitated or implemented. It begins with national, state, and local programs currently available in the SOI region. Promising practices that provide benefits are described next. While many of these programs are located in other parts of the country, some have also been implemented
in the SOI region. While all of these programs have at least some component related to capital access, the practices cover regional collaboration and technical assistance in addition to innovative financing programs.

**Federal Entrepreneurship Funding Programs**

**US Department of Agriculture (USDA)- Business and Industry Guaranteed Loan Program**

The USDA offers loan guarantees to private banks making loans to starting or expanding businesses in rural communities. The USDA may guarantee loans to rural businesses for any business purpose including real estate projects, equipment and machinery purchases, and working capital.

The percentage of loans guaranteed by the USDA is negotiated with lenders although the maximum percentage of loans guaranteed decreases with the size of the loan. For loans of less than $5 million, a maximum of 80 percent of the loan may be backed by USDA. For loans exceeding $10 million, the USDA may guarantee a maximum of 60 percent. Interest rates are negotiated between the borrower and lender and loan terms depend on the project. For real estate purchases, loans have a maximum term of 30 years. For equipment purchases, the loan term is the lesser of 15 years or the useful life of the equipment. For working capital, the maximum term is seven years.

According to USDA data provided via a Freedom of Information Act request, between 2008 and 2011, seven businesses in the SOI region received loan guarantees with a total of $42 million through the Business and Industry Guaranteed Loan Program. These loans all went toward projects for debt restructuring of existing businesses within the region.
Small Business Administration 7a Loan Guarantees

The SBA 7a Guaranteed Loan Program allows banks to make federally guaranteed loans to small businesses. The guarantee encourages lenders to make loans to businesses that might not quite meet their underwriting terms. The 7a program guarantees 85 percent of loans up to $150,000 and 75 percent of loans over $150,000, with a maximum loan amount of $5 million (Office of the Comptroller of Currency, 2013). Loan proceeds can be used for working capital or fixed assets and real estate.

Craig, Jackson and Thomson (2007, 2008a, 2008b, 2010) have reported extensive research into the economic development effects of SBA loan guarantees. They found SBA loan guarantees were positively related to employment levels and per capita income growth. These relationships are stronger in areas with higher shares of minority populations and rural areas with less developed financial systems.

Small Business Administration 504 Loans

Unlike the SBA 7a program, which guarantees a portion of a private bank loan, the 504 is a loan program. The SBA loans funds to businesses through Certified Development Companies. In a typical deal using this program, a bank provides 50 percent of the project funding (first mortgage), the SBA 504 loan funds 40 percent (second mortgage), and the entrepreneur supplies 10 percent as equity (Mihajlov, 2012). Loans from this program can be used to fund tangible assets - real estate and equipment. The second position taken by the SBA loan and the smaller portion funded by the bank reduce the bank’s risk, making it more likely that it will lend to an entrepreneur.
**US Small Business Administration (SBA)- Microloan Program**

The SBA provides funds to nonprofit, community-based organizations enabling them to offer microloans for small businesses. Nationally, the average microloan is $13,000 with an interest rate between 8 and 13 percent (Small Business Administration, 2012). The maximum amount for SBA microloans is $50,000 and the maximum term of the loan is six years. To qualify for SBA funding for microloans, community organizations must demonstrate experience in lending to small businesses and in offering technical assistance, including business training.

According to the SBA’s 2012 listing of supported microfinance institutions, six micro-lenders operate in Wisconsin but only one exists in Illinois and serves the Chicago metropolitan area exclusively. Thus, the Rockford metropolitan area is served by the SBA’s microloan program from the Chicago Office.

Two institutions in Wisconsin offer microloans to at least one county in the SOI region. The Wisconsin Women’s Business Initiative Corporation offers microloans statewide, primarily to female business owners. Impact Seven Inc. is a community development corporation offering microloans in Rock County and counties outside the SOI region. Information on outputs specific to the region or various loan programs was not available.

**US Department of the Treasury - Small Business Lending Fund (SBLF)**

The SBLF lends money to community banks that provide loans to small businesses. Eligible community banks have less than $10 billion in assets and make loans of less than $10 million to businesses with less than $50 million in revenue (US Department of the Treasury, 2013a). Banks initially repay SBLF loans at a maximum interest rate of five
percent and the interest rate decreases to one percent for banks that increase their small business lending activity by one-tenth or more.

In Wisconsin, 13 financial institutions with 55 locations receive SBLF funds. In Illinois, 22 financial institutions with 251 locations receive SBLF funds. According to a monthly transactions report, a total of $395 million in SBLF funds were loaned to 32 financial institutions in Illinois and Wisconsin as of December 31, 2012 (US Department of the Treasury, 2013b).

**State Entrepreneurship Funding Programs**

**Wisconsin Women’s Business Initiative Corporation**

The Wisconsin Women’s Business Initiative Corporation (WWBIC) makes business loans between $1,000 and $100,000 for up to six years. In 2012, WWBIC assisted 397 businesses with startup, expansion or sustainability. In the organization’s loan portfolio, 45 percent of businesses provide services either to businesses or consumers, excluding restaurants, healthcare, and childcare. Nineteen percent of businesses in WWBIC’s loan portfolio are in manufacturing or construction firms. To qualify for a loan from WWBIC, applicants must demonstrate knowledge in managing a business in their industry. Workshops on subjects such as business planning and money management are available for applicants lacking business experience.

WWBIC accepts male clients although the organization’s primary clientele are women. WWBIC receives funding from the SBA for its microloan program but information on the amount and use of funds was not available. WWBIC has eight client businesses in the SOI region, most of whom, in the SOI region, are located in Racine. These included a
transportation business, a business services consultant, and a web-based retailer of home décor products (WWBIC, 2012).

Wisconsin Angel Network

The Wisconsin Angel Network matches entrepreneurs with angel investors statewide. Through the network’s Deal Flow Pipeline, registered entrepreneurs submit one-page summaries of their businesses including the customer problem addressed, annual net revenues, amount of capital the entrepreneur seeks, a list of current investors, the business’ target market, and marketing strategy. Using the Gust software platform, angel investors browse business profiles and select businesses appropriate for their area of expertise and investment needs. In 2011 alone, members of the Wisconsin Angel Network made more than 80 investment deals (Wisconsin Angel Network, 2012).

Wisconsin Housing and Economic Development Authority

The Wisconsin Housing and Economic Development Authority (WHEDA) offers several loan guarantee programs for small businesses. WHEDA defines eligible small businesses as businesses located in Wisconsin with fewer than 250 employees that will create or retain jobs but cannot obtain conventional financing at reasonable terms. The WHEDA Small Business Guarantee program insures up to half of loans with a principal of less than $1.5 million for eligible businesses.

A similar Agribusiness Guarantee program exists for businesses using raw agricultural commodities to develop new products (e.g., a cheese manufacturer creating a new flavor of cheese) or purchase new equipment that adds value to the product. A third program, the Contractors Loan Guarantee, provides working capital for businesses with fewer than 250
employees with a contract by a federal, state, or local government agency for work within the state.

In 2012, Ktown Transportation in Kenosha received a loan from the Participation Loan Program (WHEDA, 2013). In 2011, businesses in the SOI region did not receive any WHEDA funding (WHEDA, 2012). However, in 2010 a vinyl products manufacturing company in Racine received capital from the Small Business Guarantee Program (WHEDA, 2011).

*Illinois Department of Commerce and Economic Opportunity- Advantage Illinois*

Advantage Illinois is a (introduced 2011) set of programs that improves access to capital for businesses across Illinois. A Capital Assistance Program collects funds from the state government and private banks to provide a pooled reserve for insuring loans for small businesses. This reserve protects banks against losses from loans of amounts less than $1 million to businesses with fewer than 500 employees, for terms of less than five years.

Under the Participation Loan Program, banks identify viable small businesses owned by women, minorities, and disabled veterans, and the state government provides loans in partnership with banks. Advantage Illinois also includes an Invest Illinois Venture Fund that provides additional capital to starting or expanding Illinois-based businesses that demonstrate potential for high growth in expanding markets. The Invest Illinois Venture Fund offers awards of less than $1 million or 25 percent equity.

*Illinois Finance Authority- Rural Development Loan Program*

The Illinois Finance Authority (IFA) partners with private lenders to offer loans to businesses creating or retaining jobs in rural communities with populations less than
IFA finances a maximum of 75 percent of project costs with the remainder provided by a bank. The loans have a fixed interest rate between two and six percent and a maximum term of 10 years for purchases of fixed assets. The loan term is the lesser of 10 years or the useful life for equipment purchases. According to a list of projects on IFA’s website, there are no current projects using Rural Development Loans in Boone and Winnebago County.

Local-Regional Capital Programs in the SOI Region

Stateline Angels- Rock County, Wisconsin and Winnebago County, Illinois

Stateline Angels is a group of angel investors located along the Illinois-Wisconsin state line. The organization prefers making investments of at least $250,000 to emerging businesses in industries such as business services, software, and biotechnology. Stateline Angels only invest in businesses perceived as having high growth potential and they expect applicants to identify business opportunities worth at least $50 million in revenues (Stateline Angels, 2011).

Business Lending Partners- Racine County Economic Development Corporation

Business Lending Partners (BLP), Racine County Economic Development Corporation’s Business Finance Division, offers several revolving loan funds (RLF) for businesses that will create or retain local jobs within Racine County. A deal that involves a RLF typically is funded 50% by a bank, 40% by the RLF, and requires a 10% equity stake from the borrower.

Terms and interest on loans using BLP’s revolving loan funds vary with the unit of government participating and the fund used, but most funds have a minimum interest rate of two to four percent over a maximum term of five years. Of the eight revolving loan funds
offered by BLP, four are federally-funded through the Economic Development Administration or Community Development Block Grants. Three are funded through local government resources, such as a Tax Increment Financing district. Private sources, primarily by local banks, capitalize the final RLF. In 2011, BLP approved seven loans for a total of more than $4.5 million. The resulting business projects had total investment of $34.2 million (Racine County Economic Development Corporation, 2012). BLP also provides SBA 504 loans, funded through the federal government.

BLP looks for community benefit when determining projects to fund (Carolyn Engel, personal communication). Benefits can come in the form of additional jobs or in the redevelopment of blighted areas. About 90 percent of RLF loan referrals are from local banks. BLP makes an effort to educate lenders on the RLF products available. Businesses are referred to other organizations such as a local SBDC or SCORE chapter for technical assistance.

Kenosha Area Business Alliance

The Kenosha Area Business Alliance (KABA) is the lead economic development agency for Kenosha County. KABA has a division that makes loans to businesses creating or retaining jobs in Kenosha County through several revolving loan funds in partnership with private lenders. As of the end of 2012, KABA had a total of about $28.8 million available in eight funds (Kenosha Area Business Alliance, 2012).

The share of the revolving loan fund in financing business loans varies with total project cost. For example, KABA financed 75 percent of a $110,000 microbrewery project. Four manufacturing companies that borrowed from the revolving loan fund in 2011 had projects
of between $1 million and $3 million in costs and received between 40 and 50 percent financing from KABA (Kenosha Area Business Alliance, 2012).

There are three main sources of deal flow for KABA funds: local banks looking to strengthen marginal deals, businesses wanting to relocate to the area, and previous borrowers (Richard Rodenbeck, personal communication). Businesses are referred to other organizations for technical assistance. KABA is prohibited from management participation.

Rockford Local Development Corporation

The Rockford Local Development Corporation (RLDC) is a certified development company focused on providing debt financing to small businesses, primarily in the Rockford area. Unlike BLP in Racine or KABA in Kenosha, RLDC’s sole focus is on small business financing. RLDC manages three RLFs and is a SBA 504 loan provider. The three RLFs have a total capitalization of approximately $3.5 million, with about 95% of those funds currently loaned (John Phelps, personal communication). RLDC will do a small amount of technical assistance with some potential borrowers but refers many clients to the local SBDC.

Accion Chicago

Accion is a micro lender based in Chicago. They offer loans up to $20,000 to start-ups and up to $50,000 for established businesses. They also offer small ‘credit builder’ loans between $500 and $2,500. Credit builder loans are for those who need to build a credit history or recover from a poor credit history (www.accionchicago.org).
Accion recently expanded its geographic reach to the entire state of Illinois. In the Rockford region, they engage the Rock Valley SBDC located at EIGERLab as a remote lending office. They do not offer loans to businesses in Wisconsin.

**Summary of Locally Available Capital Sources**

These examples represent a sample of loan funds currently available in the SOI region. Revolving loan funds are available in all six counties. Appendix F provides details about the loan funds currently in operation. Table 2 summarizes the loan products offered by various resources in the SOI region. As a general rule, financing is more available in the boxes marked X.

Table 2. Available Financing Amounts by Capital Source

<table>
<thead>
<tr>
<th>Capital Source / Capital Required</th>
<th>Startups</th>
<th>Early Stage Business</th>
<th>Mature Businesses (&gt; 5 years)</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Less than $20k</td>
<td>$20k - $200k</td>
<td>More than $200k</td>
</tr>
<tr>
<td>Banks - Commercial Loan</td>
<td></td>
<td>X</td>
<td></td>
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<tr>
<td>Banks - Line of Credit</td>
<td></td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>Angel Investors</td>
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<tr>
<td>Accion</td>
<td>X</td>
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<tr>
<td>* RLDC RLF</td>
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<td>X</td>
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<tr>
<td>* County RLFs</td>
<td>X</td>
<td>X</td>
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<tr>
<td>* City RLFs</td>
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<tr>
<td>* State of IL</td>
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<tr>
<td>Venture Capital</td>
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<td></td>
</tr>
<tr>
<td>Crowdfunding</td>
<td>X</td>
<td></td>
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</tr>
</tbody>
</table>

* Most RLFs and most State programs require an identical match from another lender for the $ they provide. In addition, many have job creation requirements.

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3 Brian McIntyre (Rock Valley College SBDC) and Dan Cataldi (EIGERLab) developed this matrix.
Local-Regional Technical Assistance Programs in the SOI Region

Launch Box

Launch Box is a partnership of nine agencies in Racine County, WI. The organization provides assistance to small businesses and potential entrepreneurs. According to its website (launchboxracine.com), "Launch Box is a business development resource that helps entrepreneurs and small businesses reach the next stage of their professional journey.... Our promise to small businesses and the City of Racine community includes:

- An ultra-specific, laser focus on the economic success of Racine and its entrepreneurs.
- Connects entrepreneurs with nine specific partners who provide a comprehensive range of support and resources.
- Reduces the entrepreneurial learning curve by acting as an ombudsman with Racine's city agencies.
- Helps entrepreneurs maintain critical focus during the entire entrepreneurial process.

Launch Box connects entrepreneurs with partners that provide the following services:

- Business planning
- Capital providers
- Product development
- Human resources
- Sales and marketing

EIGERlab

EIGERlab is a business and innovation incubator in Rockford, IL with several onsite technical assistance partners that provide services to tenants and other small business clients in the area. These partners include Rock Valley College, SCORE, US Department of Commerce Export Center, Northern Illinois University, the Illinois Small Business
Development Center (SBDC), the International Trade Center (ITC) and the Procurement and Technical Assistance Center (PTAC).

EIGERlab has capabilities that most incubators cannot provide. It offers product design and development, product analysis and rapid prototyping through various 3D scanning and printing technologies. These services allow entrepreneurs to produce prototypes of products in a variety of materials or even use multiple materials in a single product.

EIGERlab is developing into a more full service entrepreneurial support organization. It has adopted the GrowthWheel approach to entrepreneurial support. This approach was implemented following a realization that most of the service providers housed within EIGERlab did not effectively communicate with each other. Funders of SBDCs, SCORE, PTAC, etc., require the local offices to report on various metrics. GrowthWheel provides a common language and assessment that assists clients and providers in better defining growth parameters. These various independent service entities now are able to work collaboratively to achieve short-term business growth and results.

GrowthWheel brings the service providers together to focus on the short term goals of the business. An initial meeting with an entrepreneur produces a standardized ‘footprint’, or description of the business and its needs -- regardless of which provider has first contact. This footprint can then be shared with other providers so they can quickly identify solutions without starting over with the entrepreneur.

The GrowthWheel process quickly identifies solutions to help entrepreneurs achieve success with short-term goals. In some cases, the process can prepare a business to approach a bank for financing after just a few hours of discussion.
Another way that EIGERlab provides high value assistance to a business at a low cost is the ‘C-Team’ approach. C-Team is a holistic approach to quickly solving a business problem. They bring together a number of local experts based on the business issue. The experts might bring human resources, legal, financial, engineering, or other expertise. Experts agree to participate in the process at no charge, which takes 2-3 hours of their time.

The process begins with the entrepreneur taking 15-20 minutes to explain the problem. Following this introduction, the experts discuss potential solutions based on their skills and expertise. Occasionally, the business and an expert will enter into a business relationship following the meeting, but that is not the goal of the process.

**Promising Practices From Outside the SOI Region**

Promising practices were identified that show promise for success in the region through a review of academic and professional literature focused on entrepreneurial support. Additional practices became apparent in interviews with stakeholders.

**Promising Practice - Collaboration across Geographic Boundaries**

*Appalachian Regional Commission.* The Appalachian Regional Commission (ARC) formed the Entrepreneurship Initiative in 1997 because of concerns for the region’s future and cutbacks in declining sectors in timber, textiles, and tobacco. An “early adopter” to the economic development strategy focusing on entrepreneurship, the project garnered input from public and private stakeholders as well as commitment to the strategy by each governor and state program manager in 13 states.

The types of programs provided include access to capital, technical assistance and training, incubators, and entrepreneurship education. An evaluation of the initiative, led by
Rural Policy Research Institute’s (RUPRI) Center for Rural Entrepreneurship (2008, 3-4), found the regional impacts from the Entrepreneurship Initiative to be:

- A more entrepreneurial economy with more than 1,700 businesses created.
- A more skilled and educated workforce with more than 11,000 students and teachers trained.
- Jobs created by expanding businesses at a maximum public cost of $4,000 per job created.

**Promising Practice – Collaboration with Leadership Commitment**

*Network Kansas.* The Governor’s office along with more than 1,500 community and business leaders identified key components for the state’s new economic revitalization strategy. The Kansas Economic Growth Act of 2004 launched The Kansas Center for Entrepreneurship, which then evolved into Network Kansas. The purposes of this organization are to accelerate economic and community development. The tasks include:

- creation, review and recommendation of policies to support entrepreneurs in traditional corporate, government, non-profits and universities in Kansas;
- a centralized web portal and call center for entrepreneurs seeking assistance through a seamless resource clearinghouse;
- leading statewide collaborative efforts between educational and outreach resources; fund management and funding assistance ensuring distribution to qualified entrepreneurs;
- providing the necessary expertise, education and economic resources at the appropriate time during business development activities (Network Kansas, 2012).
Promising Practice – Community Fund Development

*Startup Kansas E-communities*: Individual community involvement includes the ability to fund and support local economic development through a statewide fund development and management program. In 2006, Startup Kansas began by providing matching grants and unsecured loans. Entrepreneurship Community funding programs or E-communities provide an additional funding source. E-communities can be a single town, cluster of towns, or an entire county that raises seed money through donations from individuals or community businesses for local entrepreneurs.

Now in its fifth year, the E-communities program has grown from six communities to 30. Partnerships invested approximately $4.7 million in the first four years and estimate that the funds will generate $33 million in investments for Kansas businesses. All types of capital sources fund startups, expansions, or retention of businesses. The sources include:

- the partner loan/ grant from Startup Kansas or E-community;
- bank loans for down payments, private capital lent by a bank or family member;
- private capital invested in return for equity;
- additional public capital loaned or granted from sources such as Certified Development Companies, Regional Foundations, USDA, city/county microloans or revolving loans; and
- owners carry the amount of capital to buy the business and business investment by the owner, such as equipment or real estate.
Promising Practice - Fund Development

Invest Nebraska: Committing resources to win and manage funding sources require professionalism and leadership talent. Structured flow of support and resources to make loans must be in place with practices that make the process achievable for all stakeholders.

With severe cutbacks in community block grants, supporting business development in the state of Nebraska required a new funding source. An application in June 2011 to a US Treasury funding program offered state small business development funds for commitment to underserved populations and distressed areas.

Awarded funds became the basis for the Nebraska Progress Loan Fund (NPLF), providing loans for commercialization. The field staff is responsible for marketing the program, creating the financial package, negotiating, and structuring the financing deal. Level of risk is the highest consideration and priorities are influenced by bank and investor actions. NPLF loan award decisions take one month and are assessed based on leverage, distressed or underserved areas, job creation and job quality.

Outputs specific to the NPLF were not available but Invest Nebraska has supported 15 businesses in total (Invest Nebraska, 2013). Most of the businesses receiving capital from Invest Nebraska are within an agricultural industry cluster. Supported businesses include sellers of agricultural products such as goat cheese and bales of hay, software developers creating programs for managing farm energy and supply use, and a mixed animal veterinary hospital.

Promising Practice - Revolving Loan Funds after Lender Refusal

Idaho Innovation Center (IIC), Idaho Fall, Idaho: Early stage companies can leverage the traditional lending turndown into a funding opportunity with support from business
development resources. Criteria for funding selection include a refusal letter from a bank or private lender and an emphasis on creating jobs. IIC returns to the lenders to ask for partial participation if IIC covers a percentage of the loan amount. The interest rate is prime lending rate plus 1-5 percent from 60 days and up to five years. A revolving loan fund of $1 million helps with equipment purchases or other needs. The minimum loan is $1,000 and maximum amount is $250,000.

**Promising Practice – Community Development Finance**

*Bootstrap Montana* offers one-year, zero-interest loans of $5,000 to $20,000 to businesses that have operated for at least one year. Short-term loans provide resources necessary for businesses to grow without burdening entrepreneurs with long-term debt. Borrowers use these loans to expand business sales and marketing activities. Uses of bootstrap loans include hiring a salesperson or presenting at a trade show. To qualify for a bootstrap loan, an applicant must present a letter of recommendation from a financial institution, legal counsel, or CPA. Businesses participating in the program must submit quarterly unaudited financial statements showing how loan proceeds were spent.

**Promising Practice – Targeted Business Assistance**

The State of Iowa provides low-interest loans to for-profit businesses with less than $4 million in annual gross income owned by resident women, racial minorities, and people with disabilities. The loans have a maximum of $50,000 over five years at less than five percent interest. Free one-on-one counseling is offered when applying for loans. In addition, businesses meeting the state’s definition of a Targeted Small Business receive notification of state agencies’ bids for goods and services 48 hours before they are made
public, providing unique opportunities for loan recipients to become government contractors (Iowa Department of Inspections and Appeals, 2012).

Promising Practice – Counseling during the Loan Application Process

Community Capital Development (CCD) in Seattle brings together three organizations that provide funding and technical assistance to entrepreneurs. Seattle Economic Development Association (SEDA) administers USDA and SBA loan funds. SEDA is a certified Community Development Financial Institution (CDFI) since 2009. One associate of CCD, the Seattle Economic Development Fund, is a certified CDFI since 1998 and administers a $6 million loan fund through various programs.

Another associate organization, Seattle Business Assistance Center (SBAC) provides small business consulting services, training and networking. SBAC operates three centers: the Washington Women’s Business Center, the South Sound Women’s Business Center, the Northwest Women’s Business Center and the Washington Statewide Minority Business Enterprise Center (MBEC).

CCD requires potential borrowers to attend sessions where they learn about available technical assistance, training programs, and the loan application process. ‘Business assistance officers’ help guide loan applicants through the process by assisting them in developing business or marketing plans, cash flow and other financial projections, and assembling and completing the required documentation (seattleccd.com). The loan documents are then referred to appropriate lending officers for review.

Promising Practice – Equity Investment Support

The Minnesota Department of Employment and Economic Development provides tax incentives for angel investors and venture capitalists providing capital to targeted
businesses. An individual income tax credit of a maximum $125,000 per year is offered to angel investors making investments of at least $10,000 in small, local technology firms. Another tax credit is available to venture capital investors providing capital to borderline businesses who target markets outside of Minnesota. Eligible investors may receive a maximum of a 45 percent tax credit on investments for a maximum of $112,500 per year.

As of 2010, the latest year with available output measures, the Angel Investment Tax Credit supported 258 angel investors and 67 certified businesses received investment (Nelson & Isaacson, 2011). Of the 67 businesses, the industry sectors most likely to receive investments were medical devices and equipment (15 businesses), software (14), and biotechnology (9) (Nelson & Isaacson, 2011). The total amount of angel investments made pursuant to the tax credit program was $28 million as of 2010 (Nelson & Isaacson, 2011).

**Promising Practice - Crowdfunding**

A relatively recent funding alternative that is growing in popularity for small businesses and microenterprises as an equity approach is crowdfunding - the process of raising money from a group of people. Crowdfunding models include those for financial return (equity and lending) as well as for projects that appeal to the personal belief of the funder (donation and reward). Crowdfunding expands the “friends and family” stage, adding investment from people unknown to the entrepreneur.

While ‘donation and reward’ crowdfunding has gone on in the past in the US, equity and lending crowdfunding is expanding. The Crowdfunding Act, signed as a component of the Jumpstart Our Business Startups (JOBS) Act signed on April 5, 2012 by President Obama has opened opportunities for entrepreneurs and business starts by removing regulatory barriers to raising capital from investors. The amended rules allow entrepreneurs and new
ventures to solicit funding with limited Security and Exchange Commission (SEC) filings, and with limited opportunities to advertise and promote the offering (Anthony, 2012).

**Promising Practice – Venture Capital**

*Venture Development Organizations (VDO)*

Accelerating the development of high-growth, innovation-based firms is a key strategy for 21st century economic development. Working with the State Science and Technology Institute, the EDA supports creation of a national network of venture development organizations to build capacity for supporting innovation and entrepreneurship in distressed regions. Venture development organizations, such as JumpStart in Northeast Ohio and Ben Franklin Technology Partners in Pennsylvania, provide a variety of services that directly benefit small businesses, including access to capital, expert business assistance, and network development.

*Regional Innovation Acceleration Network (RIAN)* assists in the creation of high growth companies, provides expert business assistance, facilitates financial investments and accelerates technology commercialization. Through this investment, EDA supports the identification of best practices in cultivating regional innovation and entrepreneurship, measuring the economic impacts of activities designed to support these objectives, and providing assistance to regions interested in establishing venture development organizations to support business development (National Economic Council, 2012; RIAN, 2012).

*SecondMarket*

*Second Market* is the largest secondary market for alternative investments, including private company stock, limited partnership interests, auction-rate securities, bankruptcy
claims, collateralized debt obligations, residential and commercial mortgage-backed securities, asset-backed securities, warrants/restricted stock and whole loans. Founded in 2004, New York-based, SecondMarket has over 40,000 participants including global financial institutions, regional and community banks, hedge funds, private equity firms, mutual funds, corporations and other institutional and accredited investors. Services were launched initially for restricted securities in public companies. Expansion to the next set of asset classes included venture-backed companies, community banks, and fund managers. (SecondMarket, n.d.).

Most recently, SecondMarket created a partnership with AngelList, a crowdsourcing platform for entrepreneurs and angel investors. The partnership allows for making investments as small as $5,000 in startup companies. For a modest investment, early-stage companies can create a more diversified portfolio for venture capitalists (Wong, 2012).

**Alternative Equity Funding Methods**

Less formal methods for acquiring capital to enhance and grow new business startup plans involve leveraging committed customers or loyal supporters. Individuals provide the financial means to help the businesses grow and in turn receive product or service vouchers for the product or service. Alternative methods include Community Supported Enterprises and Revenue-Based Financing (see Appendix E).

**Promising Practice – Networking Resources**

*The Capital Network (TCN), Austin, TX:* Networking resources together offers an array of assistance to support entrepreneurs and develop access to capital potential. Including more than 15,000 firms, financing resources and business assistance organizations, TCN is one of the nation’s largest seed and venture capital networks. A database includes business
experts to help firms with structuring deals, marketing, and management. Entrepreneurs pay $750 for a six-month membership and investors pay $1,250 per year for membership in the network. Angel investor receptions are organized by TCN, which showcases three high-growth potential startup companies.

**Promising Practice - Community Supported Enterprises**

The Community Supported Enterprise (CSE) functions like Community Supported Agriculture (CSA) model. CSA brings a community of individuals together, pledging support to a farming operation by signing up to receive a weekly delivery of farm products. The farmers receive the capital needed to maintain and grow their crops and members receive their share of food throughout the growing season.

With difficulty in finding capital without losing control of the company once the business is up and running, individuals can establish a relationship with a growing business by purchasing coupons from the company that are redeemable at stores for the product. This provides the business with necessary upfront capital, helping to ensure long-term viability.

Most often, the CSE supports and preserves local communities, through a combination of charitable and investment contributions, especially when the community commits to supporting the new startup. A memorandum of understanding reinforces the partnership between the new business and the community, outlining the arrangement’s principles and circumventing misunderstandings. Details of CSE arrangements and examples of implementation are seen in The Preservation Trust of Vermont (PTV).

The PTV promotes many CSEs within the state. One example includes a local restaurant that avoided closure by collecting $1,000 contributions from customers who were repaid
via quarterly $90 coupons for the restaurant. Another restaurant collected $5,000 each from 32 investors and repaid them in savings of 25% on all meal purchases at the restaurant for five years.

Vermont’s CSEs also include a general store where customers may pay $15 annually to receive discounts on all purchases (Preservation Trust of Vermont). These examples show that CSE arrangements are scalable for the business’ capital needs and preferred repayment schedule.

**Promising Practice - Multi-jurisdictional, public-private entrepreneurship development program**

Organizations in the Region of South Denmark have coordinated efforts to improve access to capital for small businesses (European Entrepreneurial Region, 2011). Public sector entities partnered with the private sector to expand entrepreneurship in the region. A regional council coordinates political support from various jurisdictions. The South Danish Regional Business Development Centre is responsible for entrepreneurial counseling services. A youth entrepreneurship program focuses on expanding entrepreneurship efforts. Finally, Danfoss, a large industrial corporation founded in the region is committed to provide expertise and resources to entrepreneurship development.

Several investment organizations are designed to help small businesses. Business Angels Southern Denmark is a network of regional investors who systematically identify local opportunities for investment in start-ups. The Fund for Growth Promotion in southern Denmark was created by the Growth Forum to provide loans to entrepreneurs in remote areas of the region and venture capital to entrepreneurs working within the prioritized field of health and welfare technology. Danish Growth Fund has a local division that creates new growth companies by providing venture capital in collaboration with
private partners and Danish financial institutions. Science Ventures Denmark A/S, owned by the University of Southern Denmark, invests in high-tech business development. Finally, the Investment Fund of South Jutland provides loans to SMEs in Southern Jutland.

There are also several technical assistance programs in the region. *Capital through Counseling* is an initiative where a capital coach helps an SME in need of finance and acts as a personal advisor. The Regional Business Development Centre in a similar fashion works to raise the profile, importance, and value of intellectual property rights to ensure growth and freedom to operate. South Danish Technological Innovation represents one of the largest Danish government approved innovation incubator schemes implemented to ease access to capital.

Danfoss is the private sector partner. They conduct an annual internal business plan competition to boost employees’ innovation and entrepreneurial skills. There are plans to add business plan competitions for students in 2013 and an ‘entrepreneur park’ was started to nurture technology-driven entrepreneurs.

**Promising Practice – Entrepreneurial Support Organization**

The Kentucky Highlands Investment Corporation (KHIC) is an entrepreneurial support organization that provides a diverse set of financing options, including equity and debt financing. In addition, KHIC offers entrepreneurial training and managerial assistance. In some cases, employees of KHIC take an active management role in the companies in which they invest.

KHIC has operated for more than 40 years and has developed into an effective organization with broad community support. An evaluation of the organization provided some ‘lessons learned’ from the successes of KHIC (Markley and Barkley, 2003):
1. Focus on the entrepreneur and the enterprise, rather than the capital used to support the enterprise. “...assistance includes recognizing the weaknesses in an entrepreneur’s set of management skills and plugging the gaps in the management team, even with KHIC staff” (p. 14).

2. Build a committed and skilled staff. “The quality of support provided to entrepreneurs is a function of the quality of staff assembled in the Kentucky Highlands organization. Individual staff members demonstrate a strong commitment to both the southeastern Appalachian Kentucky region and the organization itself” (p. 14).

3. Focus on grantsmanship. “KHIC has been successful in tapping a number of federal programs that provide greater flexibility in responding to an entrepreneur’s needs” (p. 15).

4. Develop an active and supportive board of directors. The KHIC board provides continuity, averaging over 17 years of service. There are strict participation requirements for serving which creates a high level of commitment. The board challenges staff to be innovative and take risks, understanding that failure is sometimes the cost of risk-taking.

5. Partner with other development organizations in the region and across the nation. “Partnerships are a key to KHIC’s success, allowing the organization to share risk, extend its geographic reach, and increase the talent pool available to help entrepreneurs” (p. 16).

These lessons also bring caveats. First, because the organization was formed more than 40 years ago, KHIC received substantial federal funding that is no longer available. Capitalization of a similar organization would provide significant challenges today.

Second, KHIC does not work with very early stage entrepreneurs. “The organization does not attempt to identify potential entrepreneurs who articulate an interest in starting their own business but who present no concrete business idea. There continues to be a gap in the region in providing this deal flow development activity” (Markley and Barkley, 2003, p. 13).

**Promising Practices – Economic Gardening**

Economic Gardening is an approach to economic development that focuses on growing from within through entrepreneurship. Entrepreneurs receive technical assistance in the
form of research about markets, competitors and industry trends. The goal is to provide small business owners the type of information available to much larger corporations so they can make better strategic decisions.

Promising Practices – Fund Management Service

_Evanston Business Investment Corporation (EBIC):_ EBIC uses a private university as a fund management support service. Operating a seed capital fund as a service for the clients of Evanston Business & Technology Center, Northwestern University, Evanston, IL, EBIC is co-located with the incubator but operates independently. Two seed funds were developed by EBIC, which is locally organized and founded as a non-profit. A matching investment from another source is required to participate. Typical investments in incubator companies & other local businesses are between $50,000 and $150,000. The clients of the incubator also receive financial advice.

Promising Practices – Expertise Pooling

_The Plato Initiative_ is a program being implemented throughout Europe to increase the frequency and depth of networking between business owners/managers. The Plato program forms small groups (about 10-20 members) of business managers. The group typically consists of primarily small business owners/managers with two representatives of larger companies. The group progresses through a two-year program that includes formal and informal meetings, seminars, and individual counseling. Participants learn management skills from peers and develop business and personal connections that frequently lead to commercial opportunities.
Conclusions and Recommendations

The data collected suggest that entrepreneurship is strong in the SOI region from some perspectives. Business start rates in each of the counties are significantly higher than the Illinois/Wisconsin averages. However, business closure rates and declines in the number of business establishments in the SOI region indicate that entrepreneurs struggle to succeed and more support for entrepreneurs in the region could have significant positive impacts.

Indicators show financial capital resources are used in the region. Data from SBA lending indicate that the value of loans made is slightly above the statewide per capita averages. However, a survey of bankers completed for this report revealed that this source could be more fully utilized. More than one-third of banks indicated that they do not use the SBA loan programs.

In addition to SBA lending programs, several business finance programs exist in the region. State direct loan or loan guarantee programs include Wisconsin Women’s Business Initiative Corporation, Wisconsin Housing and Economic Development Small Business Guarantee program, Advantage Illinois Capital Assistance Program, and Illinois Finance Authority Rural Development Loan Program. Revolving Loan Funds exist in every county in the SOI region.

While access to capital is essential for new and expanding businesses, financing programs are only part of a larger regional entrepreneurship system. According to Holley, "a Regional Entrepreneurship System includes:

- a coordinated system of easily accessible technical assistance and training;
• local communities that value entrepreneurs and link them to appropriate services;
• access to appropriate capital;
• the formation of clusters that provide sector-specific assistance; and
• a process for gathering information about gaps in the system and developing policy and new services to address those gaps” (2005, p. 7).

While this report concentrated on access to capital, a regional entrepreneurship support system should have a broader focus. In some areas, such as small business counseling, a regional approach is beginning to take hold. More effort will be required in other areas.

The findings from this analysis of access to capital suggest recommendations on four issues: research, training, capital sources, and regional coordination. Each recommendation addresses either a weakness in the current system or it builds on emerging strength in the region. The implementation of these recommendations can help create a positive climate that encourages startups or expansions by 2nd stage companies.

Research

Small Business Financing Experience

The vast majority of academic research on small business lending is based on large datasets such as the Kauffman Firm Survey. These data are collected from surveys that ask about the source and amount of financing that small businesses apply for and/or obtain. These data are useful for understanding trends, but do not help understand the experiences, decisions, and detailed needs of specific entrepreneurs.

A research effort focused on entrepreneurs’ experiences with obtaining capital in the SOI region would identify obstacles faced in financing efforts and could help formulate remedies. It is well-documented that entrepreneurs rely heavily on personal savings or
debt and bank loans. (see Appendix C). However, the process that they go through when deciding to invest personal funds or take on debt is not well-understood but would help considerably in tailoring financing packages. What analysis do entrepreneurs rely on? How prepared are they when approaching banks? What are the experiences of entrepreneurs who have attempted but failed to obtain financing? The answers to these questions could guide policymakers in creating effective financing strategies but have not been addressed adequately in previous research especially for remote and rural regions.

**Recommendation #1:**

*Initiate a research effort focused on the financing experiences of small businesses.* A well-designed mixed methods study would produce generalizable results useful in designing better products and services to help entrepreneurs grow or expand their businesses. Exploratory qualitative research, e.g. interviews with entrepreneurs and/or financial institutions, followed by a quantitative survey with greater reach could test the generalizability of the qualitative findings. The findings then can be used to design new funding opportunities in the region or to expand access to existing programs.

*Angel Investor Identification*

Angel investors are “wealthy individuals, typically fellow entrepreneurs, willing to invest in the very early stages of a venture development” (Morrissette, 2007, p. 52). In 2012 the median angel investment was approximately $600,000 (Angel Resource Institute and Silicon Valley Bank, 2013). Prior to the investment, the companies receiving the funds had a median valuation of about $2.5 million. In the Great Lakes region, internet and health care companies received almost 60 percent of angel investment deals in 2012.
Angels typically invest in industries they know (Morrissette, 2007, p. 52) and many are hands-on investors who meet frequently with the entrepreneurs they finance. Consequently, over 75% of angel investors invest in companies within 50 miles of their residence.

Stateline Angels is an investment group in the SOI region. According to their website, “members are a group of successful business executives and professionals in the Stateline region of Winnebago County, Illinois and Rock County, Wisconsin” (www.statelineangels.com/history). The description of their philosophy matches well with what was found in the academic literature:

Stateline Angels is an angel investor organization that provides investment capital to start-up and early stage companies. Members who choose to invest may also lend their operational experience to enhance the chance of success to the ventures. We are dedicated to fostering growth in the Stateline area and upper Midwest region by assisting individuals in the development of successful businesses.

Local business development experts believe that there are many other potential angel investors in the region. Entrepreneur magazine suggest four places to search for angel investors:

- **Universities:** According to Bob Tosterud, Freeman Chair for Entrepreneurial Studies at the University of South Dakota, angel investors tend to hover near university programs because of the high level of new business activity they generate. He advises that if you are looking for money, call the nearest university that has an entrepreneurship program, and make an appointment to speak with the person who runs it. Generally, he says, such people can point you in the direction of angels.

- **Business incubators:** According to the National Business Incubation Association (NBIA), there are about 1,000 business incubators in North America. At first glance, incubators appear to be the mere bricks and mortar facilities that offer entrepreneurs reasonable rents, access to shared services, exposure to professional assistance and an atmosphere of entrepreneurial energy. But according to NBIA
president and CEO Dinah Adkins, many business incubators offer formal or informal access to angel investors.

- **Venture capital clubs**: The tremendous wealth created through the commercialization of technology, as well as the robust stock market of the 1990s, have resulted in a large number of angel investors who have begun to formalize their activities into groups or clubs. These clubs actively look for deals to invest in and their members want to hear from entrepreneurs looking for capital.

- **Angel confederacies**: Some angels, shunning the formality of a venture capital club, band together in informal groups that share information and deals. Members of the group often invest independently or join together to fund a company. So-called confederacies are not easy to find, but once you locate one member, you gain access to them all, a number that could top 50 investors. (A Guide to Angel Investors, n.d.)

*Entrepreneur* goes on to suggest sources for finding angel investors:

1. Many chambers of commerce host a venture capital group. Many such groups have a chamber affiliation.

2. Small Business Development Centers often know of local angel investor groups.

3. Accounting firms may provide entrepreneurial services and know of local angel investors.

4. Similarly, lawyers may provide services to wealthy individuals willing to invest locally.

5. Professional venture capitalist may be aware of an angel investor group.

6. Regional or state economic development agency may know of an angel investor group.

7. Local business publications often write about angel investment groups and may be aware of their activity.

8. "Principle Shareholders" section of initial public offerings (IPO) prospectuses for companies in the area will identify local business persons with significant cash outs.

9. The executive director of a trade association may be aware of investors who specialize in a specific industry.

10. The president of a local bank or lenders at a larger commercial bank may know of angel groups because companies that have received an equity investment are good candidates for a loan.
Recommendation #2:

These resources represent a starting point in a systematic effort to identify angel investors in the SOI region. A snowball sampling technique would broaden the reach beyond the original set of interviewees. The survey findings could then be shared on a website or other media with potential entrepreneurs. In addition, discussions with the angel investors regarding interests in specific business ventures could inform strategies by development practitioners in identifying potential entrepreneurs. Angel investors could also help by indicating the types of information they find most useful and the formats they prefer. All of this information could then lead to informational and training efforts for entrepreneurs in the future as shown next.

Training and Technical Assistance

Technical assistance and training are especially important because many early stage entrepreneurs do not have skills required to prepare to obtain financing. National surveys of entrepreneurs indicate that entrepreneurs lack the financial analysis skills required to apply successfully for financing. Many do not even approach banks, assuming they will be denied funding. As such, potentially successful businesses are underfunded.

Small businesses could benefit from access to more sophisticated market analyses, assistance with financial calculations and projections, and information about federal, state and local financing programs. Coordination between service providers would also benefit the region. These services range from face to face counseling to internet or phone-based

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4 Snowball sampling employs a question at the end of each interview asking the participant to identify others who might have information related to the study.
services. Examples of programs in other regions could be implemented in the SOI region to improve entrepreneurial support.

The Region of South Denmark provides a ‘capital coach’ to entrepreneurs in need of finance. The coach acts as a personal advisor helping the company to attract capital. Taking that concept a step further, the Idaho Innovation Center provides business development resources along with an internal source of potential capital for entrepreneurs who have been refused by a bank. The Kentucky Highlands Investment Corporation is an entrepreneurial support organization that provides entrepreneurial training and managerial assistance along with a diverse set of financing options, including equity and debt financing.

Network Kansas provides a service to entrepreneurs to help them connect with appropriate service providers, including a toll free phone number staffed by referral coordinators. During an initial phone call, the coordinators learn about the entrepreneur's business and needs. The coordinator then researches the issues and calls potential service providers. They connect the entrepreneur with the service providers and follow them through the process, making sure their needs are met.

Community Capital Development (CCD) in Seattle brings together three organizations that provide funding and technical assistance to entrepreneurs. CCD requires potential borrowers to attend sessions where they learn about available technical assistance, training programs, and the loan application process. ‘Business assistance officers’ help guide loan applicants through the process by assisting them in developing their business or marketing plans, cash flow and other financial projections, and assembling and completing the required documentation (seattleccd.com).
There are also successful examples of peer-to-peer mentoring programs that could be successfully implemented. The Plato Initiative is a program implemented throughout Europe to increase the frequency and depth of networking between business owners/managers. This program forms small groups (about 10-20 members) of business managers. The group typically includes small business owners/managers and representatives of larger companies. Participants learn management skills from their peers and gain business and personal connections that frequently lead to commercial opportunities.

Within the SOI region, EIGERlab’s C-Team is a holistic approach to quickly solving a business problem. They bring together a number of local experts based on the business issue. The experts might bring human resources, legal, financial, engineering or other expertise to help an entrepreneur solve a difficult business problem.

A coordinated system of technical assistance is beginning to take shape in the SOI region. Other organizations are adopting the GrowthWheel approach that EIGERlab has undertaken. Representatives from Gateway Technical College in Sturtevant, WI and the Whitewater Innovation Center at UW-Whitewater are undergoing the training and will begin implementing it with clients by the end of 2013. As of May 2013, there were 18 certified GrowthWheel business coaches in the SOI region.

Several training opportunities were identified in the current research effort. Many revolving loan fund (RLF) managers in the region (especially in smaller communities) need more sophisticated knowledge about financing alternatives to support local businesses. Most likely, business counselors at SBDCs and other places could use better financial
training as well. The survey of bank personnel disclosed that many are not aware of some of the local, state, and federal resources available to small businesses.

The National Development Council (NDC) provides Economic Development Finance Professional certification training. This training is designed for people who manage RLFs and work with businesses and developers on financing. The certification requires a significant investment of time (four week-long courses) and money (NDC charges $1,250 for each week-long course). In some regions such as South Dakota, banks or other organizations provide financial support to bring NDC training to a region. In 2013, the Ohio Department of Development hosted EDFP courses at a reduced rate of $685 per course. A program such as this could be implemented in the SOI region.

Smaller, more targeted education efforts could also help. Seminars or webinars on specific aspects of business lending could educate RLF managers about opportunities to stimulate small business growth in their regions. Representatives from SBA or USDA could present seminars about their loan programs targeted to either bank loan officers or entrepreneurs.

At the same time, it is imperative that entrepreneurs and 2nd stage company managers be prepared when seeking loans. They must understand their cash flow potential, understand markets, and have the supply chain under control if they expect lending institutions to provide financing. Since running a small business can consume all of their time, it is important that they have access to technical and management expertise on a readily accessible and affordable level. Reviewing the current capacity of SBDCs and other agencies in the region to provide this level of support would be useful. It would also be
useful to determine whether small businesses are fully utilizing these services and identify obstacles to more widespread utilization.

**Recommendation #3.**

Building on findings from the survey of banking personnel, an organized training effort could be created in the SOI region aimed at better informing participants about opportunities to provide financing but also to create better collaboration among loan personnel. For instance, a meeting of finance and development personnel in Rockford demonstrated that many participants had not met and were not knowledgeable about how their specific programs could work with other possibilities. Building a more seamless lending environment could make it easier for entrepreneurs to obtain financing.

Likewise, continuing and expanding the SOI SourceLink website could help business starts. Providing basic information about businesses in the region and the locations of financial programs would help minimize the transaction costs associated with business starts. This website could be maintained in a development office, university agency or other regional group.

Creating training programs for entrepreneurs to improve their financial management, marketing, and other functions is important. An inventory of these programs could be taken and then reviewed by a panel of small business and/or 2nd stage company managers to identify missing links. The SOI partnership has made great strides in linking these various technical services but it may be time to step back and evaluate whether there are still missing links.
Small Loan Sources

Small businesses have a special need for loans of less than $50,000. Banks are hesitant to make small loans because of the high administrative costs relative to the revenue generated. Based on interviews and survey findings, banks willing to lend smaller amounts – often through lines of credit – treat them as personal loans, relying on the borrowers’ personal credit score and collateral.

There are a few other sources of small loans. Accion Chicago makes loans (up to $20,000 for startups and $50,000 for expansions) and they recently expanded their territory to include the Rockford region but do not make loans in Wisconsin. Local RLFs are often willing to loan smaller amounts but may be more difficult to find.

The State of Kansas provided seed funding for local communities to create loan funds. Entrepreneurship Community funding programs or ‘E-communities’ provide an additional funding source. E-communities can be a single town, cluster of towns, or an entire county that raises seed money through donations from individuals or community businesses for local entrepreneurs.

In Idaho, early stage companies can leverage the traditional lending turndown into a funding opportunity with support from business development resources. Criteria for funding selection include a refusal letter from a bank or private lender and an emphasis on creating jobs. The Idaho Innovation Center returns to the lenders to ask for partial participation if IIC covers a percentage of the loan amount.

Bootstrap Montana offers one-year, zero-interest loans of $5,000 to $20,000 to businesses that have operated for at least one year. Short-term loans provide resources necessary for businesses to grow without burdening entrepreneurs with long-term debt.
Borrowers use these loans to expand business sales and marketing activities. Uses of bootstrap loans include hiring a salesperson or presenting at a trade show.

Crowdfunding is an emerging source of small business lending. Entrepreneurs can post funding requests on websites such as kickstarter.com and are then matched with investors. Currently, only loans and donations are permitted by US regulations. Regulatory changes in progress will allow entrepreneurs to tap into crowdfunding for equity investments.

Recommendation #4.

The sources of capital can be improved by taking advantage of existing resources and attracting new resources to the region. Revolving loan funds are underutilized, especially in the more rural parts of the region. Better communications among lending agencies could lead to collaborative projects and/or could reduce the transaction costs for small borrowers. Likewise, coordinated efforts in the region to bring in new lending agencies such as Accion could lead to additional lending opportunities for startups and/or expansions. Any efforts to reduce the risks faced by lending institutions and/or increasing the profitability of making these types of loans should improve the economic climate.

By the same token, it is important that borrowers are well-prepared when they make an application as was noted in the section on training. Time spent making information available about potential markets, population trends, and similar intelligence could improve the finance conditions.

Regional Partnerships and Coordination

Holley (2005) suggests setting up a ‘policy network’ to support entrepreneurship in a region. “A policy network is composed of entrepreneurs, Entrepreneur Support Organizations, government officials, policymakers and others who are interested in
developing effective entrepreneurship policy” (p. 56). Several models of successful regional coordination of entrepreneurship support networks could serve as models in the SOI region. For example, an organization in southeastern Kentucky has had strong successes in specific areas, including regionalism.

The Kentucky Highlands Investment Corporation (KHIC) covers 22 counties in southeast Kentucky. In addition to providing a variety of financing options for small businesses, they coordinate activities of service providers across the region. For KHIC, “partnerships are a key to KHIC’s success, allowing the organization to share risk, extend its geographic reach, and increase the talent pool available to help entrepreneurs” (Markley and Barkley, 2003, p. 16). They also have created national partnerships with organizations such as the National Community Capital Association and the National Cooperative Bank. In their view, these local and national partnerships strengthen entrepreneurial support in the region beyond what could be achieved by one organization.

Many successful entrepreneurial support efforts are housed in multi-county regional organizations. This is especially important for less densely populated areas where economies of scale are more difficult to achieve. These organizations can create larger loan funds which provide interest income to support their operations. However, the composition of the SOI region creates obstacles that complicate creating a single umbrella organization.

First, the region crosses a state line raising several funding challenges. For example, an angel investor network that crossed the state border was discussed by SOI participants. This effort was derailed by private investors not interested in working across state lines. This issue could be explored further and might be attractive to funding agencies.
Second, the mix of urban and rural areas can bring challenges. Rural participants may feel they are not a priority in regions with more urban centers. Building long-term coalitions may be more difficult in these cases. However, it is now more common for banks in metro areas to have operations in more remote locations. These situations may make it easier to build linkages.

Despite the lack of a regional umbrella organization, informal regional collaboration is happening. Programs such as the GrowthWheel, started at EIGERLab, are spreading to organizations across the SOI region. More recently, representatives from Gateway Technical College in Sturtevant, WI and the Whitewater Innovation Center at UW-Whitewater are being trained and are implementing the program with clients. As of 2013, there are now 18 certified GrowthWheel business coaches in the SOI region.

EIGERLab also pioneered the FastPitch entrepreneurial competition in the region, hosting the first competition in Rockford in 2007. The competition features three minute ‘pitches’ by entrepreneurs where they promote the merits of their business ideas. In 2012, both UW-Parkside in Kenosha and the UW-Whitewater Innovation Center started competitions. In 2013, an ‘All Star’ event was added, bringing together the top competitors from Rockford, Whitewater, and Kenosha.

Recommendation #5.

Early signs indicate that regional programs such as FastPitch and GrowthWheel will have a positive impact on business financing in the region. Expanding these programs to new locations will be a positive step. Other areas are also trying new approaches and it is important that the SOI region keep up to speed with the latest successful practices.
Especially important is that the region work as a unit. This is critical for the small agencies in less densely populated areas. To succeed, they will have to collaborate with and build on the efforts of the larger cities and regional centers. Linking the financial centers with development agencies that work with small businesses will be key to a prosperous future.

Path Forward
These four areas (research, training, capital sources, and regional coordination) are interrelated. Training RLF managers will help business projects have access to currently available funds. By expanding on the informal regional coordination currently underway, experienced RLF managers can mentor newer, less experienced managers. The research outlined can help better design training programs that help current entrepreneurs more effectively tap into existing traditional finance sources as well as guide policymakers toward effective programs underway in other areas.
### Organizations Referenced

<table>
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<td>SecondMarket</td>
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<td>Startup Kansas</td>
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<td>The Capital Network (TCN), Austin, TX</td>
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<td>The Preservation Trust of Vermont</td>
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<td>United States Department of Agriculture</td>
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<td>United States Small Business Administration (SBA)</td>
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<td>Wisconsin Women’s Business Initiative Corporation</td>
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SBA Office of Advocacy, September 2011 www.sba.gov


Appendix A: Entrepreneurial Demographics

There has been considerable research on characteristics of entrepreneurs. Global Entrepreneurship Monitor (GEM) conducts an annual entrepreneurial assessment worldwide and the 2011 report (Kelley et al., 2011) provides a profile of entrepreneurs in the US. According to GEM, in 2011 more than 55 percent of the adult population believed they had the ability to start a business. Significantly, approximately 36 percent of the US population stated that they recognized entrepreneurial opportunities. Of that 36 percent, nearly one-third said that a fear of failure dissuaded them from starting a business. Financial considerations contributed significantly to this fear.

The GEM report describes entrepreneurially active persons as those who have taken steps to start a business or are running a business less than 42 months old. The US had a ‘Total Entrepreneurial Activity’ (TEA) rate of 12.3 percent in 2011 and the rate was somewhat higher for men (13.6 %) than women (10.8 %). This might indicate that female-focused entrepreneurship programs in the SOI could reach an underserved population.

While younger people tend to have higher levels of entrepreneurial intent and established business owners tend to be older, rates of early stage entrepreneurs (those of primary interest in this report) do not vary significantly between age groups (Figure A1). The nascent entrepreneurship rate peaks for the population between 25 and 34 (early career) and drops off only slightly for mid-career adults. New business ownership rates are relatively consistent for age groups between 25 and 54. This suggests that entrepreneurship programs need not be age specific. Interestingly, TEA rates even out between the genders for entrepreneurs above 45 years old.
According to the GEM report (Kelley et al., 2011), entrepreneurs usually come from wealthier households. The TEA rate is 14.4% for the wealthiest one-third of households compared to 11.3% for the lowest one-third income category. Significantly, entrepreneurs in wealthier households tend to be much more opportunity driven (i.e., starting a business because of a market opportunity) as compared to necessity driven (i.e., starting a business to pay immediate bills). This is important because opportunity driven businesses tend to have greater potential than necessity driven businesses.

Education is correlated with entrepreneurial activity (Kelley et al., 2011) and college graduates are twice as likely to engage in entrepreneurial activity as those without a high school education. Similar to income, those with higher education levels are much more
likely to be opportunity driven entrepreneurs while those with no high school diploma are more likely driven by necessity.

More recently, Walzer and Blanke (2013) studied business starts in more than 800 Midwestern counties. They found significant correlations between business starts and females 25 to 34 years of age, pre-retirees between 55 and 64 years, Hispanics, unemployed, and small farm operators. They also report a positive correlation with population density. The findings are especially interesting for the SOI because both Illinois and Wisconsin were included in the study. Essentially, the research found that pre-retirees, Hispanics, farm operators with less than 250 acres, unemployed, and females between 25 and 34 years of age were positively associated with growth of business starts between 2004 and 2007 (pre-recession period) as a percentage of businesses in 2004. The analysis included adjustments for quality of life, population density, wealth in the county, and related variables.

SOI Region Demographics

Considering the geographic business challenges and the entrepreneurial profiles presented above, it is important to examine the demographics of the SOI region. With a few exceptions, the region is relatively rural. Rock and Walworth counties in Wisconsin and Boone County, IL each have population densities of between 180 and 220 persons per square mile. Winnebago County, IL (dominated by the City of Rockford), Kenosha County, WI (City of Kenosha), and Racine County, WI (City of Racine) each have densities between 575 and 625 persons per square mile. By comparison, Cook County, IL (City of Chicago) has a density of 5,500 persons per square mile. Many studies (e.g., Markley, 2007 and Walzer & Blanke, 2013) describe challenges of promoting entrepreneurship in rural areas.
As described above, entrepreneurs have higher education levels. College graduates are twice as likely to be entrepreneurially active compared with those with less than a high school education. This is another challenge in the SOI region where the percentage of residents with bachelor’s degrees or higher is lower than statewide averages, especially in the more rural counties in the region.

The age composition in the SOI region closely matches Illinois and Wisconsin overall with the share of the population in pre-career, early career, late career, and retired nearly identical with the two states (Figure A2). One quarter of the population is less than 18 years, slightly more than one-third is 18 to 44 years old, one-fourth is age 45 to 64 years, and the remaining 13 percent is more than 64 years of age.

Figure A2: Population Breakdown By Age, 2010

<table>
<thead>
<tr>
<th>Age cohort</th>
<th>SOI Region</th>
<th>Illinois &amp; Wisconsin</th>
</tr>
</thead>
<tbody>
<tr>
<td>19 &amp; Under</td>
<td>27.91%</td>
<td>26.99%</td>
</tr>
<tr>
<td>20-44</td>
<td>31.77%</td>
<td>33.56%</td>
</tr>
<tr>
<td>45-64</td>
<td>27.27%</td>
<td>26.56%</td>
</tr>
<tr>
<td>Over 64</td>
<td>13.04%</td>
<td>12.89%</td>
</tr>
</tbody>
</table>


Even though the SOI region's age demographics mirror the two states overall, trends in the SOI region between 2000 and 2010 differ from the two states (Figure A3) and these trends provide insights in entrepreneurship and workforce opportunities.

The SOI region's school-age population (under 18) increased 1.8 percent even as the same cohort decreased in Illinois and Wisconsin. The region lost young professionals (age 18-44) but did not lose nearly as many, proportionally, as Illinois and Wisconsin combined, which is encouraging because this age group has been shown to include potential entrepreneurs in some cases (Kelley et al., 2011). However, the SOI region also had more people retire or has a higher percentage nearing retirement than the two states.
Of special interest is the relatively large increase in proportion of residents between 45 and 65 years of age during the past decade. This trend reflects a natural aging of the population but also suggests shortfalls in the future workforce in the region as those past 45 years of age approach retirement age.

The projected population changes in the SOI region to 2020 are consistent with those in Illinois and Wisconsin (Figure A4) but in both cases, a growing number of seniors (over age 64) will retire and a shortage of experienced workers (age 45 to 64) is expected. Woods and Poole Economics (2012) predicts increases in the population who will start careers and could partially offset losses from retirements, but the growing number of potential retirees exceeds the growth of all other cohorts combined. In some cases, those past 65 years will continue to work, especially if the average wage increases due to a relative shortage of workers.
While past research on determinants of business starts (Walzer & Blanke, 2013) shows that the 54 to 65 age group is positively and significantly related to business starts, improvements in job prospects for traditional employment opportunities may tend to attract those who, otherwise, might consider starting businesses and therefore adversely affect the stock of potential entrepreneurs. In either case, the age groups that included entrepreneurs in the past will probably find better employment prospects in traditional employment sources in the foreseeable future.

Figure A4: Projected Population Change 2010-2020


While the demographics of the SOI region suggest that it might struggle with entrepreneurial activity, business statistics indicate that it is doing well. The next section presents business trends showing that entrepreneurial activity is high in the region relative to the statewide averages.
Business Trends in SOI Region

*Business Dynamics Statistic Data* (US Census, 2012), including small businesses in operation less than 5 years was used to construct a profile of business activity in the SOI region between 2004 and 2007 in Illinois, Wisconsin and the US to compare trends in number of business establishments (Appendix B has data variable definitions). The data provide a perspective on the composition of businesses both by size and years of operation and can illustrate trends in business starts of new, small establishments. The years selected avoid influences of the Great Recession and better reflect likely experiences in future business activities.

*Economic Importance*- Small businesses account for a significant portion of the economy in terms of both number of establishments and employees. In Illinois and Wisconsin, over 93 percent of all establishments are small businesses with fewer than 50 employees. More than one-third of all business establishments are startups (less than five years old) and over one fifth of all businesses are microenterprises with five or fewer employees.

Small businesses are also significant employers. Two-fifths of employees in all establishments work in small businesses, mostly in businesses that have operated for more than five years. This group is also a target for services by the SOI partners.

*Job Creation*- In addition to being major sources of current employment, small business startups also create many jobs. In Illinois and in the United States, slightly over half of all jobs created by business establishments came from small businesses, defined as businesses with fewer than 50 employees (Figure A5). Within the small business category, microenterprises created one-tenth and startups one-third of all jobs. As small businesses expand, they become more important for job creation; small businesses with fewer than 50 employees accounted for a higher percentage of all jobs created than microenterprises.
However, small businesses in Wisconsin created fewer jobs on average than in Illinois. Improving access to capital for small business expansions may improve the job creation rates of small businesses especially in Wisconsin.

Figure A5: Percentage of Total Job Creation Attributed to Small Business, 2004-2007

Business Activity and Structure in the SOI Region

Business Starts- During the pre-recession period (2004-2007), the SOI region compared relatively well in business starts as measured by the percentage of businesses starting during this period relative to number of business starts in 2004. This finding suggests a positive environment for starting businesses. Using the BizMiner dataset\(^5\) between 2004

and 2007 the average county in the SOI region had business starts equal to 9.5 percent of the total number of business establishments in the region in 2004 (Figure A6).

The average county in Illinois and Wisconsin combined had a business start rate of 5.6 percent. A t-test of differences between group means, after adjusting for size and variance in both groups, shows that the six counties in the SOI region had significantly higher business start rates on average than did Illinois and Wisconsin overall. In fact, the six counties in the SOI region are all within the top 16 percent of counties in the two states for pre-recession business start rates.

Figure A6: Business Start Rate Comparisons

<table>
<thead>
<tr>
<th>Location</th>
<th>2004-2007 Total Starts as Pct. Of 2004 Total Firms</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Two-State Average</strong></td>
<td>5.6%</td>
</tr>
<tr>
<td>Wisconsin average</td>
<td>6.8%</td>
</tr>
<tr>
<td>Illinois average</td>
<td>4.7%</td>
</tr>
<tr>
<td><strong>SOI Average</strong></td>
<td>9.5%</td>
</tr>
<tr>
<td>Racine, WI</td>
<td>11.9%</td>
</tr>
<tr>
<td>Kenosha, WI</td>
<td>11.8%</td>
</tr>
<tr>
<td>Winnebago, IL</td>
<td>8.5%</td>
</tr>
<tr>
<td>Walworth, WI</td>
<td>8.4%</td>
</tr>
<tr>
<td>Boone, IL</td>
<td>8.1%</td>
</tr>
<tr>
<td>Rock, WI</td>
<td>8.0%</td>
</tr>
</tbody>
</table>


The higher performance of the SOI counties compared with other counties extends across the retail, wholesale, finance/real estate, services, and construction sectors. In most cases, SOI counties surpassed the two-state average start rate individually as well as collectively.

However, the SOI counties also differ markedly in some respects. Kenosha County had major increases in agriculture-related businesses with a start rate in this sector double
the SOI average and four times the two-state average. Racine County had a start rate in retail nearly twice as high as the average county in Illinois and Wisconsin. The counties of Racine and Kenosha also had large increases in numbers of construction firms.

Walworth County did not lead the region in start rates in any industry but it had a business start rate higher than the average county in every industry except manufacturing and mining. The Rockford metropolitan area--Boone and Winnebago counties-- had a business start rate in transportation and utilities nearly twice as high as the average county in the two states. Both individually and therefore collectively, counties in the SOI region have been conducive to entrepreneurial activity.

Business Closures- According to the BizMiner dataset, counties in the SOI region also had high rates of business closures (Figure A7). In every industry except mining, the average SOI county had a higher closure rate than the average county in Illinois or Wisconsin. A comparison of the averages using a t-test showed that the SOI region had significantly higher closure rates in the construction and service sectors than the average county in Illinois and Wisconsin. Thus, the SOI region had lost a substantial number of businesses in construction and services even before the recession.
**Figure A7: County-Level Average Business Closure Rates 2004-2007**

<table>
<thead>
<tr>
<th></th>
<th>SOI Region</th>
<th>Illinois &amp; Wisconsin</th>
<th>t Value*</th>
</tr>
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<tr>
<td>Agriculture</td>
<td>8.0%</td>
<td>5.9%</td>
<td>1.97</td>
</tr>
<tr>
<td>Small Businesses</td>
<td>7.8%</td>
<td>5.9%</td>
<td>1.96</td>
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<tr>
<td>Mining</td>
<td>2.3%</td>
<td>10.8%</td>
<td>-1.10</td>
</tr>
<tr>
<td>Small Businesses</td>
<td>4.0%</td>
<td>14.8%</td>
<td>-1.27</td>
</tr>
<tr>
<td>Construction</td>
<td>13.8%</td>
<td>11.9%</td>
<td>3.08*</td>
</tr>
<tr>
<td>Small Businesses</td>
<td>14.1%</td>
<td>12.0%</td>
<td>3.32*</td>
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<tr>
<td>Manufacturing</td>
<td>12.0%</td>
<td>10.2%</td>
<td>1.27</td>
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<tr>
<td>Small Businesses</td>
<td>13.9%</td>
<td>11.0%</td>
<td>1.47</td>
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<tr>
<td>Transportation &amp; Utilities</td>
<td>15.5%</td>
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<td>1.64</td>
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<tr>
<td>Small Businesses</td>
<td>15.9%</td>
<td>13.6%</td>
<td>1.36</td>
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<td>Wholesale Trade</td>
<td>11.9%</td>
<td>10.2%</td>
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<td>Small Businesses</td>
<td>12.8%</td>
<td>10.3%</td>
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<td>Retail Trade</td>
<td>15.9%</td>
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<td>16.4%</td>
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<td>Finance &amp; Real Estate</td>
<td>13.0%</td>
<td>10.9%</td>
<td>0.89</td>
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<td>Small Businesses</td>
<td>13.0%</td>
<td>11.5%</td>
<td>0.59</td>
</tr>
<tr>
<td>Services</td>
<td>14.9%</td>
<td>12.4%</td>
<td>3.23*</td>
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<tr>
<td>Small Businesses</td>
<td>15.2%</td>
<td>12.6%</td>
<td>3.51*</td>
</tr>
<tr>
<td>All Industries</td>
<td>13.9%</td>
<td>11.3%</td>
<td>4.89*</td>
</tr>
<tr>
<td>Small Businesses</td>
<td>14.3%</td>
<td>11.5%</td>
<td>5.13*</td>
</tr>
</tbody>
</table>

*Statistically significant at less than 5%

Source: The Brandow Company, BizMiner.

Furthermore, changes at the state level do not explain these losses because the SOI region's closure rate was proportionally higher than in Illinois and Wisconsin. The small business closure rate in SOI counties was three percentage points higher than the two-state average, a difference that is statistically significant at less than 1 percent. Even though the closure rate for mining companies was 8 percentage points lower in the SOI than the average county in Illinois or Wisconsin, this difference was not statistically significant because the number of mining businesses varied widely among counties. The higher than

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6 In the BizMiner dataset, a small business is defined as a business establishment with only one site and less than 25 employees.
average business closure rates in SOI counties indicate special issues that may threaten small businesses and a possible need for remedial action. High business closure rates pressure local development practitioners even more to foster business starts and replace businesses lost through closures.

The high closure rates in the SOI region are reinforced by variations among counties (Figure A8). In terms of total business closures across all industries, Boone County had the lowest closure rates in the region (11.9 percent) and Racine County had the highest (15.6 percent) from 2004 to 2007. In most industries, the individual SOI counties, individually, had a higher business closure rate than Illinois and Wisconsin overall. Exceptions were found in manufacturing, transportation and utilities, and financial services. Walworth County was the only county in the region with a lower manufacturing business closure rate than the two-state average (7.8 percent compared to 10.2 percent). In the financial services industry, Boone County had a lower closure rate than the two-state average (3.8 percent compared to 10.9 percent).
The SOI region lost more businesses, proportionally, in the recession than the states of Illinois and Wisconsin overall. According to Walls & Associates, Inc.’s *National Establishment Time Series* database, the total number of business establishments in the SOI region decreased 5.6 percent between 2007 and 2009 (latest data available), compared with 5 percent decline in Illinois and 4.5 percent decline in Wisconsin (Figure C9).

According to the National Establishment Time Series, in both the SOI region and Illinois and Wisconsin overall, a majority of establishment closures during the recession involved resident-owned businesses with less than 10 employees (Figure A9). In the SOI region, 84 percent of the 3,134 establishments lost between 2007 and 2009 were resident-owned businesses with less than 10 employees. In Illinois and Wisconsin overall, 69
percent of all establishments lost were resident businesses with less than 10 employees. Of more significance regarding employment, the SOI region lost five establishments with more than 500 employees during the recession—equal to 16 percent of the region’s total number of major employers pre-recession.

Figure A9: Change in Business Establishments, 2007-2009

<table>
<thead>
<tr>
<th>SOI Region</th>
<th>Illinois and Wisconsin</th>
</tr>
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<tr>
<td>Change</td>
<td>%</td>
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<td>Total Establishments</td>
<td>-3,134</td>
</tr>
<tr>
<td>Noncommercial</td>
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<tr>
<td>Nonresident</td>
<td>-275</td>
</tr>
<tr>
<td>Resident</td>
<td>-2,660</td>
</tr>
<tr>
<td>Below 10 employees</td>
<td>-2,332</td>
</tr>
<tr>
<td>10-99 employees</td>
<td>-299</td>
</tr>
<tr>
<td>100-499 employees</td>
<td>-24</td>
</tr>
<tr>
<td>500+ employees</td>
<td>-5</td>
</tr>
</tbody>
</table>


*Business structure*- The distribution of businesses in the SOI region matches statewide and national patterns and highlights the significance of small, locally-owned businesses. According to the National Establishment Time Series, 81 percent of all businesses in the SOI are resident-owned businesses with less than 10 employees, which matches the *Business Dynamics Statistics* data mentioned previously (see Figure A10). The proportions of nonresident-owned establishments, large locally-owned establishments, and noncommercial establishments in the SOI region are congruent with the business structure statewide and nationally.
Figure A10: Business Structure in 2009

<table>
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<tr>
<th></th>
<th>SOI Region</th>
<th>Illinois and Wisconsin</th>
<th>US</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>% of Total Establishments</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Noncommercial</td>
<td>5.9%</td>
<td>6.5%</td>
<td>6.2%</td>
</tr>
<tr>
<td>Nonresident</td>
<td>3.8%</td>
<td>4.0%</td>
<td>3.6%</td>
</tr>
<tr>
<td>Resident</td>
<td>90.2%</td>
<td>89.5%</td>
<td>90.2%</td>
</tr>
<tr>
<td>Below 10 employees</td>
<td>81.2%</td>
<td>80.2%</td>
<td>82.6%</td>
</tr>
<tr>
<td>10-99 employees</td>
<td>8.4%</td>
<td>8.6%</td>
<td>7.2%</td>
</tr>
<tr>
<td>100-499 employees</td>
<td>0.5%</td>
<td>0.6%</td>
<td>0.4%</td>
</tr>
<tr>
<td>500+ employees</td>
<td>0.05%</td>
<td>0.1%</td>
<td>0.05%</td>
</tr>
</tbody>
</table>


The SOI region proportionally has an equal number of establishments as Illinois and Wisconsin overall in most industries. In both the SOI region and the two states, the three industries with the largest share of establishments were construction, education and health services industries. In total, the SOI counties have a slightly larger proportion of construction establishments than Wisconsin and Illinois and a slightly smaller share of establishments in education and health services. The one industry with the most notable differences between the SOI region and the two states is Information, where the SOI region has a higher concentration of establishments than Wisconsin and Illinois. Considering establishments in all SOI counties and all industries, the region largely has the same industrial mix as the two states overall.

The industry mix of individual counties in the SOI varies. All SOI counties had a larger concentration of construction establishments than the two states overall, but Rock County had the largest share of construction establishments at nearly 25 percent. Each county had an above-average concentration of establishments in the Information industry but Winnebago had the largest share in this industry (10 percent compared to 5.5 percent). In the manufacturing industry, Kenosha County had a below-average establishment share.
and Boone County had an above-average share (15.4 percent compared to 10.4 percent in Illinois and Wisconsin combined). The distribution of industries in each county is important because it partially indicates the opportunities for new business development. (Source: US Census Bureau, 2010 County Business Patterns)
### Appendix B: Definitions of Financing Options

<table>
<thead>
<tr>
<th>Business Life Cycle Stage</th>
<th>Finance Type</th>
<th>Source</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Zero</td>
<td>Debt or Equity</td>
<td>Friends and Family</td>
<td>The first and most popular source for capital comes from people who know the entrepreneur best and are inclined to agree to make the investment. As most startups have a high tendency to fail, the downside and risks should be clear. Only those who can afford to lose should invest. Depending on the amount raised and the size of the opportunity, a convertible note with a discount and cap is the best approach to mitigate risk for this type of financing (Wilson, May 30, 2011).</td>
</tr>
<tr>
<td>Zero - One</td>
<td>Debt</td>
<td>Microfinancing</td>
<td>Microfinance is a system that offers loans to individuals who are emerging entrepreneurs or self-employed but part of underprivileged or low income communities. People obtain loans when they cannot go through other traditional financial sources such as commercial banks or moneylenders (Hoje et al., 2009).</td>
</tr>
<tr>
<td>One</td>
<td>Debt</td>
<td>Customer Financing</td>
<td>In some cases, customers can be a source of funding. Customer funders do not have the financial requirements that banks impose. They can prove market fit for the product/service offered, improve the quality, and provide credibility with other customers. An early customer may provide the funding in exchange for a tailored product to meet its needs, resulting in a product not suited for a broader market. A scalable product is one sold “as is” rather than building a product for a fee. Customer financing can create a culture of “fee for services” (Wilson, June 20, 2011).</td>
</tr>
<tr>
<td>One</td>
<td>Debt or Equity</td>
<td>Community Supported Enterprises</td>
<td>This model is based on the Community Supported Agriculture model, which brings a community of individuals together, pledging support to a farming operation, by signing up to receive a weekly delivery of farm products. The farmers receive the capital needed to maintain and grow their crops and members receive their share of food throughout the growing season. The Community Supported Enterprise functions similarly. It may be difficult to find capital without losing control of the</td>
</tr>
<tr>
<td>Business Life Cycle Stage</td>
<td>Finance Type</td>
<td>Source</td>
<td>Description</td>
</tr>
<tr>
<td>---------------------------</td>
<td>--------------</td>
<td>-------------------------------</td>
<td>-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>One or Two</td>
<td>Debt</td>
<td>Vendor Financing</td>
<td>Considered a loan, a capital-intensive startup is most likely to use this option. A new company will benefit from this approach when repayment plans can be adapted to the business’s cash flow. When bank loans are unattainable, vendor financing may provide more flexibility, extending the repayment period and reducing monthly payments (Wilson, June 27, 2011). No collateral or co-signer is necessary (Vendorfinancing.org, 2011). If unable to obtain repayment, the vendors can write down the loss as bad debt (Investopedia, 2012).</td>
</tr>
<tr>
<td>One or Two</td>
<td>Debt</td>
<td>Convertible Debt</td>
<td>The startup borrows money from an investor or group of investors with the intention of converting the debt to equity later that is specified at the time the loan is made. In return, compensation requires a discount or warrant and cap on valuation for the investor. The company believes that it will be worth more in the future, with less dilution, and lower transaction costs in issuing debt rather than equity. Investors believe that the compensation in the discount or warrant has enough value to offset the value of taking debt versus equity. Additionally, the investor is more secure since debt ranks higher than equity in liquidation. Early on, startups use convertible debt for capital needs to move quickly, with low transaction costs and the simplicity of obtaining capital in this manner rather than seed or Series A (the first round of financing for a new business venture after seed capital). This source of a capital is most useful to company growth as they become more sophisticated in the need for financing funding (Wilson, July 11, 2011).</td>
</tr>
<tr>
<td>One or Two</td>
<td>Debt</td>
<td>Capital Equipment Loans &amp; Leases</td>
<td>These loans made by banks and finance companies provide funds to acquire capital equipment. The equipment is collateral used to secure the loan. Repayments of these loans occur in three years with interest rates</td>
</tr>
<tr>
<td>Business Life Cycle Stage</td>
<td>Finance Type</td>
<td>Source</td>
<td>Description</td>
</tr>
<tr>
<td>---------------------------</td>
<td>--------------</td>
<td>--------</td>
<td>-------------</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>between 6% and 12%. At the end of the term, the company has the option of returning to the lessor or purchasing for a nominal amount. This option provides capital without diluting the value. The company can keep scarce capital resources while continuing to develop the business. Both the lender and borrower align in the risk (Wilson, August 2, 2011).</td>
</tr>
<tr>
<td>One or Two</td>
<td>Debt</td>
<td>Working Capital Financing</td>
<td>The cash consumption from day-to-day operations is what the customers owe plus inventory built minus what is owed to suppliers and employees, as well as any cash in the bank. Even though on paper the business looks profitable, the outlay of capital to produce the product and the time when the revenue come in can stall production and delay further income. These are loans to the business by banks and financing companies for necessary inventory purchases while waiting for payment from customers. Financing relies on the current inventory and the orders in hand to determine the loan amount. The structure of the loan is lines of credit and loans repaid as the money comes back into the business. The total amount available stays the same and the company can borrow it back again when it needs money.</td>
</tr>
<tr>
<td>Two or Three</td>
<td>Debt</td>
<td>Venture Debt</td>
<td>Specialized banks and finance companies provide this debt option. Terms are three years on average with interest only payments each month. When the term expires, a balloon payment for the full amount of the loan is required. Warrants provide a right to buy equity at a fixed price within a specific timeframe (usually 5 to 10 years).</td>
</tr>
<tr>
<td>Two or Three</td>
<td>Debt</td>
<td>Bridge Loans</td>
<td>Money-losing companies use bridge loans before they run out of funds when waiting to close a financing deal or sales transaction, which does not often happen. The loss rate is high and returns are not much better than venture investment, making these loans risky. As a specialized form of convertible debt, the terms of the bridge loan are standard, secured by all the business’s assets, carrying interest rates of 6% to 12%. Bridge loans are common to all businesses; however, they can be viewed as a signal of distress for the startup company (Wilson, August 15, 2011).</td>
</tr>
<tr>
<td>Business Life Cycle Stage</td>
<td>Finance Type</td>
<td>Source</td>
<td>Description</td>
</tr>
<tr>
<td>--------------------------</td>
<td>--------------</td>
<td>--------</td>
<td>-------------</td>
</tr>
<tr>
<td>Zero - One</td>
<td>Equity</td>
<td>Crowdfunding</td>
<td>An idea is funded with small contributions by a large number of individuals providing access to capital and investor protection (Startup Exemption, (n.d.)).</td>
</tr>
<tr>
<td>One</td>
<td>Equity</td>
<td>Accelerator Programs / Contests / Prizes</td>
<td>Best known accelerator programs (e.g., TechStars and Y Combinator), pioneered this approach. Founding members relocate for approximately three months to a specific location. Typically, this is an equity funding opportunity, offering between $25,000 and $30,000 in exchange for a 5-6% equity stake. These funds are sufficient for the founding team in the program and may last a bit longer than three months. The greatest value in the accelerator programs is from the mentoring and opportunity to pitch to angel investor groups at the conclusion of the program. Contests and prize competitions have increased in recent years. Entrepreneurs receive support and preparation in business plan development from the hosting organization and compete for a set amount of money (i.e., $5,000 up to $10,000). The preparation consists of brief meetings over a period of three months and culminates with a presentation to a panel of judges, often comprised of angel investors or key community and/or business leaders. The funds provided by this source are unlikely to take a business to breakeven; rather, it provides the money and connections needed to set up for the next source (Wilson, June 6, 2011).</td>
</tr>
<tr>
<td>One or Two</td>
<td>Equity</td>
<td>Preferred Stock</td>
<td>Investors and venture capitalists require any company in which they invest to issue preferred stock, as security for their equity dollars. This class of stock provides superior security since the investors have the option of taking their cost out or sharing proceeds with founders in the event of company liquidation. Among the important privileges and rights is a seat on the board of directors, information, protection of ownership percentage in future rounds, right of first refusal for common stock offerings, participation alongside common stock sale and purchase price adjustments to guard against dilution. Variation exists in how the transaction is structured. Understanding the terms for both the investor and the company are essential (Wilson, July 18, 2011).</td>
</tr>
<tr>
<td>Business Life Cycle Stage</td>
<td>Finance Type</td>
<td>Source</td>
<td>Description</td>
</tr>
<tr>
<td>---------------------------</td>
<td>----------------</td>
<td>-----------------------------</td>
<td>-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>One or Two</td>
<td>Equity</td>
<td>Mergers and Acquisitions</td>
<td>A consolidation of companies. A merger combines two companies to create a new company; an acquisition is the purchase of one company by another without forming a new company (Investopedia, 2012).</td>
</tr>
<tr>
<td>One &amp; beyond</td>
<td>Equity</td>
<td>Strategic Partnering</td>
<td>Not a permanent or legal partnership, but an agreement between two companies to achieve specific goals that will circumvent one’s weakness with another’s strength. Also called a strategic partnership (Investopedia, 2012).</td>
</tr>
<tr>
<td>Three &amp; above</td>
<td>Equity</td>
<td>Initial Public Offering</td>
<td>The first sale of private company stock to the public. An underwriting firm helps determine type of issue, price and timing for the sale (Investopedia, 2012).</td>
</tr>
<tr>
<td>One</td>
<td>Neither</td>
<td>Government Grants</td>
<td>The source of these funds does not require payback or equity stake. The application process is involved, is extensive and may come with stipulations for use, including specific use or hiring a set number of people. Small Business Innovation Research (SBIR) grants are most common, although grants from a specific department (i.e., health, energy) are available. This is not a popular form of funding and is unlikely to provide enough for the business to progress (Wilson, June 13, 2011).</td>
</tr>
<tr>
<td>One or Two</td>
<td>Revenue share</td>
<td>Revenue-based Financing</td>
<td>Often dubbed &quot;royalty-based financing&quot;, the concept is frequently used by the film and natural resources industries when investors are paid back with a percentage of gross receipts. With no dilution, no loss of control, and no fixed repayment schedule, entrepreneurs can stay focused on growing their businesses. It works like a revenue sharing agreement. This is ideally suited for early stage companies that are generating sales, but need additional capital to take full potential of their opportunities and grow as fast as possible (Jones, 2012).</td>
</tr>
</tbody>
</table>
Appendix C: Small Business Capital Usage

Public Use Microdata from the US Census 2007 Business Owners Survey (US Census, 2012) for Illinois and Wisconsin provide an indication of the types and frequency of access to the available financing resources. The survey included 47,639 respondents from Illinois and 21,310 from Wisconsin, providing a total sample of 68,949. Since respondents reported all sources from which they obtained capital, percentages do not always total 100%. Options to acquire necessary capital to develop a business in Stage 0 in the business life cycle are few and, not surprisingly, personal savings (66.6%) are the greatest source of capital. Almost one quarter of startups obtain capital through a bank loan (Figure C1).

Figure C1: Sources of Startup Capital in Illinois and Wisconsin, 2007

In the expansion phase, businesses continue to use savings as their main source of capital (27.4%). In addition, a new source of capital exists for financing business operations: profits (18.7%) (Figure C2).
The Kauffman Firm Survey (KFS) provides detailed panel data about startup firms. The KFS began collecting data in 2004 from nearly 5,000 randomly selected firms that were started in that year. With annual follow-up surveys, KFS tracks firms through time.

Robb, et. al., (2010) described the results of the KFS data from startup to surviving four year old firms in 2008. Table C1 displays the sources of capital injections at year 1 and year 4 for the firms. Almost 90 percent of all firms (3,125 of 3,564) use owner equity for at least a portion of their startup capital. These owner injections accounted for 36 percent ($28,541 of $80,359) of average capital in startup funding. A closely related source, owner debt (primarily credit cards) is used by more than one-third of startups, but this source accounts for only about 4 percent of average capital. Thus, owner equity and personal debt represent approximately 40 percent of startup capital in these firms.

Outsider debt accounts for another 40 percent of startup capital according to the KFS data. However, a smaller percentage of firms (about 40 percent) use it as a source of...
capital at startup. Major sources in this category include personal bank loans, bank business loans, and lines of credit.

Capital from ‘insider’ (friends and family) sources represents slightly more than 10 percent of average startup capital. Insider capital comes mostly in the form of loans rather than equity in the firms.

Outsider equity is rarely used by startup firms, according to the KFS data. However, when this source is used, it tends to be a significant amount of funding. Only 26 of the 3,564 firms that used capital sources accessed venture capital. However, the average investment for these firms was more than $350,000.

As firms matured, their sources of capital changed. Of the firms in the KFS sample that survived to 2008, about two-thirds used outsider debt for new capital, accounting for two-thirds of average capital injections. Less than half of these firms used additional owner equity. Owner funds (debt and equity) were approximately 20 percent of the average new capital.

Even as these firms matured, very few used outside equity as a capital source. These capital sources are used for larger injections, likely in high growth firms. The seven firms that attracted venture capital averaged over $1 million in new capital from that source.
Table C1: Source of Capital Injections for Kauffman Survey Firms

<table>
<thead>
<tr>
<th>Source of Capital</th>
<th>All Firms: 2004</th>
<th>Surviving Firms: 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Startup Capital</td>
<td>New Capital Injections</td>
</tr>
<tr>
<td></td>
<td>All Firms</td>
<td>Just Firms with Source &gt; 0</td>
</tr>
<tr>
<td>Total New Financial Injections</td>
<td>$80,359</td>
<td>$89,255</td>
</tr>
<tr>
<td>Owner Equity</td>
<td>$28,541</td>
<td>$36,134</td>
</tr>
<tr>
<td>Insider Equity</td>
<td>$1,700</td>
<td>$36,367</td>
</tr>
<tr>
<td>Spouse Equity</td>
<td>$491</td>
<td>$30,732</td>
</tr>
<tr>
<td>Parent Equity</td>
<td>$1,209</td>
<td>$35,310</td>
</tr>
<tr>
<td>Outsider Equity</td>
<td>$6,901</td>
<td>$153,608</td>
</tr>
<tr>
<td>Other Informal Investors</td>
<td>$2,793</td>
<td>$107,685</td>
</tr>
<tr>
<td>Other Business Equity</td>
<td>$1,841</td>
<td>$162,369</td>
</tr>
<tr>
<td>Government Equity</td>
<td>$466</td>
<td>$85,664</td>
</tr>
<tr>
<td>Venture Capital Equity</td>
<td>$1,454</td>
<td>$352,111</td>
</tr>
<tr>
<td>Other Equity</td>
<td>$347</td>
<td>$189,561</td>
</tr>
<tr>
<td>Owner Debt</td>
<td>$3,487</td>
<td>$11,322</td>
</tr>
<tr>
<td>Personal Credit Card–Owner Personal</td>
<td>$3,175</td>
<td>$10,587</td>
</tr>
<tr>
<td>Credit Card–Other Owners</td>
<td>$288</td>
<td>$8,995</td>
</tr>
<tr>
<td>Personal Owner Loan</td>
<td>$25</td>
<td>$15,853</td>
</tr>
<tr>
<td>Insider Debt</td>
<td>$7,633</td>
<td>$52,048</td>
</tr>
<tr>
<td>Personal Family Loan</td>
<td>$2,670</td>
<td>$28,398</td>
</tr>
<tr>
<td>Personal Family Loan–Other Owners</td>
<td>$286</td>
<td>$34,681</td>
</tr>
<tr>
<td>Business Loan from Family</td>
<td>$1,350</td>
<td>$43,909</td>
</tr>
<tr>
<td>Business Loan from Owner</td>
<td>$1,887</td>
<td>$117,804</td>
</tr>
<tr>
<td>Business Loan from Employee(s)</td>
<td>$69</td>
<td>$19,349</td>
</tr>
<tr>
<td>Other Personal Loan</td>
<td>$559</td>
<td>$29,457</td>
</tr>
<tr>
<td>Other Personal Funding</td>
<td>$812</td>
<td>$64,514</td>
</tr>
<tr>
<td>Outsider Debt</td>
<td>$32,097</td>
<td>$86,374</td>
</tr>
<tr>
<td>Personal Bank Loan</td>
<td>$10,476</td>
<td>$61,086</td>
</tr>
<tr>
<td>Business Credit Card</td>
<td>$1,394</td>
<td>$9,828</td>
</tr>
<tr>
<td>Other Bank Loan</td>
<td>$1,498</td>
<td>$65,010</td>
</tr>
<tr>
<td>Business Credit Card–Other Owners</td>
<td>$167</td>
<td>$9,694</td>
</tr>
<tr>
<td>Business Credit Cards</td>
<td>$859</td>
<td>$7,383</td>
</tr>
<tr>
<td>Bank Business Loan</td>
<td>$10,060</td>
<td>$154,043</td>
</tr>
<tr>
<td>Credit Line</td>
<td>$3,798</td>
<td>$71,429</td>
</tr>
<tr>
<td>Other Non-Bank Loan</td>
<td>$2,040</td>
<td>$120,971</td>
</tr>
<tr>
<td>Government Business Loan</td>
<td>$725</td>
<td>$84,303</td>
</tr>
<tr>
<td>Other Business Loan</td>
<td>$187</td>
<td>$63,305</td>
</tr>
<tr>
<td>Other Individual Loan</td>
<td>$259</td>
<td>$49,512</td>
</tr>
<tr>
<td>Other Business Debt</td>
<td>$634</td>
<td>$120,971</td>
</tr>
</tbody>
</table>

Source: Robb, et al., (2010) analysis of Kauffman Firm Survey Microdata. Sample includes only surviving firms over the 2004–2008 period, and firms that have been verified as going out of business over the same period. The original sample size in 2004 was 4,928.

Note: *indicates sample size is less than 7.
Mason and Stark (2004) noted that new entrepreneurs should be aware that the sources of funding each emphasize different types of information and each funding source uses different criteria when reviewing a startup’s business plan. Bankers, venture capital fund managers and business angels each probe the business plan for specific criteria with different weights. The funding proposal requires adaptation accordingly. The start-up’s viability, potential profit, downside risk, likely life cycle time, and potential areas for improvement are central issues of concern for all funding requests.

Analysis of the KFS data also showed that about 13 percent of firms in the sample applied for a loan in 2008 (Table C2) and more than two-thirds of firms received the loans. The most common reasons for denial were credit history, insufficient collateral, and requests that were too large (Robb et al., 2010).

Table C2: Borrowing Experiences of KFS Firms in 2008

<table>
<thead>
<tr>
<th>New Loan Applications</th>
<th>13.2%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan Application Outcome</td>
<td></td>
</tr>
<tr>
<td>Always Approved</td>
<td>67.6%</td>
</tr>
<tr>
<td>Sometimes Approved/Sometimes Denied</td>
<td>17.5%</td>
</tr>
<tr>
<td>Always Denied</td>
<td>14.9%</td>
</tr>
<tr>
<td>Reasons for Denial</td>
<td></td>
</tr>
<tr>
<td>Insufficient Collateral</td>
<td>42.2%</td>
</tr>
<tr>
<td>Loan Request Too Large</td>
<td>28.0%</td>
</tr>
<tr>
<td>Inadequate Documentation</td>
<td>15.6%</td>
</tr>
<tr>
<td>Business Credit History</td>
<td>33.3%</td>
</tr>
<tr>
<td>Personal Credit History</td>
<td>45.0%</td>
</tr>
<tr>
<td>Business is Too New</td>
<td>15.7%</td>
</tr>
<tr>
<td>Other</td>
<td>14.7%</td>
</tr>
<tr>
<td>Didn’t apply when needed credit because thought they would be turned down</td>
<td>17.6%</td>
</tr>
</tbody>
</table>


According to Rittenberg (2011), 24 million US businesses with five or fewer employees have capital needs of less than $35,000. Capital providers incur a number of costs when making loans related to credit checks, loan application analysis, and processing. Because of these costs, many financing programs are not cost effective for these small loans. This
poses a significant challenge in the effort to meet new small business capital needs (Rittenberg, 2011).

The research by Mason and Stark (2004) and the KFS data indicate that many business owners could benefit from technical assistance to help them in obtaining capital. Owners with knowledge about the technical aspects of their industry may not have the financial analysis skills required to obtain financing from outside debt or equity sources. Assistance from an outside expert in preparing loan applications or presentations to equity providers might allow them to succeed more often.

**Magnitude of Startup Financing**

The amount of capital required for small businesses between Stages 0 - 2 can vary significantly. Further analysis of the data from the Business Owners Survey (US Census, 2012) provides details regarding the capital needs among Illinois and Wisconsin startups. One quarter of startups require less than $5,000 and about half of startups require less than $25,000 (Figure C3). Approximately one in seven startups needs over $250,000 in capital.
When considering the industry sector classifications for startups, the Professional, Technical, and Scientific Services sector requires the least startup capital. The service sector is more labor intensive (Acs, Armington, & Zhang, 2007) which may explain why capital requirements are less than in other sectors (Table C3).

**Table C3: Startup Industry Sectors by Capital Need**

<table>
<thead>
<tr>
<th>Startup Capital Need</th>
<th>Predominate Industry Sector</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under $5,000</td>
<td>Professional, Technical &amp; Scientific Services</td>
<td>27.26%</td>
</tr>
<tr>
<td>$5,000 - $9,999</td>
<td>Professional, Technical &amp; Scientific Services</td>
<td>19.78%</td>
</tr>
</tbody>
</table>
| $10,000 - $24,999    | Construction                                     | 16.51%
| $25,000 - $49,999    | Retail Trade                                     | 13.44%
| $50,000 - $99,999    | Retail Trade                                     | 14.86%
| $100,000 - $249,999  | Retail Trade                                     | 16.38%
| $250,000 - $999,999  | Retail Trade                                     | 16.36%
| $1M+                 | Manufacturing                                    | 15.27%

Appendix D: Small Business Debt Options

Small business ventures can access four main sources of debt finance during their developing and early stages: personal (friends and family) financing; bank financing, (credit cards, lines of credit and loans); trade credit; and government/non-institutional financing. Table D1 provides an overview of the types of debt financing available for businesses by stage of development.

Table D1: Debt Financing Alternatives for Business

<table>
<thead>
<tr>
<th>Stage</th>
<th>Debt Financing Sources</th>
<th>Debt Financing Types and Documents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Development</td>
<td>Founders, friends, and family SBA loan guarantees</td>
<td>Loans, promissory notes and loan agreements</td>
</tr>
<tr>
<td></td>
<td>Equipment vendors</td>
<td>SBA guaranteed revolver or term note, notes and loan agreements</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Leases</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Promissory notes with high interest and collateralized by personal assets</td>
</tr>
<tr>
<td>Operating</td>
<td>Banks Institutional investors and private equity Equipment vendors and leasing firms</td>
<td>Debt-loan agreements and promissory notes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Mezzanine debt, convertible debt, or securitizations-notes, debentures, loan agreements, conversion agreements and warrants</td>
</tr>
</tbody>
</table>


Personal Savings

Personal investment is the most used source of capital in the initial development phase of a small business. The Small Business Administration (SBA) reports that personal savings is the number one source of start-up capital for small businesses in Stage 0 and, on average, 60% of small business firms seeking start-up capital use a combination of personal and family savings (SBA, 2011). Personal savings and resources such as credit lines that borrow against personal assets allow an owner to maintain the most control of the business (Lopez-Garcia and Aybar-Arias, 2000; Blumber and Wilko 2008). Even when
financing from personal funds is structured as a loan, financial institutions frequently view it as equity because the owner loans are subordinate to other types of financing.

Data from the US Census Business Owner’s Survey, 2007 (US Census, 2012) show that virtually all startups use savings as the primary source of capital. Depending on the amount of capital needed, the secondary and tertiary sources could vary (Table D2).

Table D2: Sources for Capital Based on Amount

<table>
<thead>
<tr>
<th>Startup Capital Need</th>
<th>Primary Source</th>
<th>Secondary Source</th>
<th>Tertiary Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under $5,000</td>
<td>Savings</td>
<td>Credit</td>
<td>Bank Loan</td>
</tr>
<tr>
<td>$5,000 - $9,999</td>
<td>Savings</td>
<td>Bank Loan</td>
<td>Credit</td>
</tr>
<tr>
<td>$10,000 - $24,999</td>
<td>Savings</td>
<td>Bank Loan</td>
<td>Credit</td>
</tr>
<tr>
<td>$25,000 - $49,999</td>
<td>Savings</td>
<td>Bank Loan</td>
<td>Equity</td>
</tr>
<tr>
<td>$50,000 - $99,999</td>
<td>Savings</td>
<td>Bank Loan</td>
<td>Equity</td>
</tr>
<tr>
<td>$100,000 - $249,999</td>
<td>Savings</td>
<td>Bank Loan</td>
<td>Equity</td>
</tr>
<tr>
<td>$250,000 - $999,999</td>
<td>Savings</td>
<td>Bank Loan</td>
<td>Assets</td>
</tr>
<tr>
<td>$1M+</td>
<td>Savings</td>
<td>Bank Loan</td>
<td>Assets</td>
</tr>
</tbody>
</table>


Friends & Family

Investment from friends and family with an established repayment plan is considered debt, as opposed to an equity position with the company, sharing profits from the firm. Friends and family may provide relatively easy to access loans, usually in addition to personal investment (Walter, 2004). Firms with a lack of tangible assets (i.e., no asset structure) tend to rely on capital from less formal means such as friends and family (Cassar, 2002).

While friends and family can provide available funding, Lee and Persson (2012) found that entrepreneurs typically use this source of funding as a last resort. It can be even more unattractive in risky ventures and in large investments that can constrain growth. In addition, imposing risks on family and friends is unappealing and has potential relationship
repercussions. In a random sample of 1,498 Illinois small business owners, only 16.5 percent reported negotiating loans from friends or family (Neely & Van Auken, 2012). In the national Kauffman Firm survey, in 2004, 15.2 percent of capital injections to new firms involved debt from individuals with personal connections to the entrepreneur (Robb et al., 2010).

**Bank Finance**

External debt financing for small firms follows the start of the business. Established and operating entrepreneurs typically seek bank financing other than bank-owned credit cards. Entrepreneurs promote their new venture by establishing a credible personal commitment to the business. Business owners should provide credible commitments and signals to the bank to increase confidence that the business is likely to succeed and be able to repay the loan even if it fails (Avery, et al., 1998; Blumberg and Wilko, 2008). Personal collateral commitments, such as home ownership or other investment property are preferred by banks (Blumber and Wilko, 2008). This has become an issue during the Great Recession when the market value of homes declined. In addition, incorporation of the business and asset secured debt increases the likelihood to receive bank capital (Cassar, 2002).

The approach to evaluating business lending by traditional financial institutions can be categorized in four ways – “financial statement lending, asset-based lending, credit scoring, and relationship lending” (Berger and Udell, 2002). Often, new businesses do not have a clear and straightforward funding arrangement, which imposes additional difficulties and costs on lending institutions and limits access to financial statement lending. Financial statement lending is when a bank loans funds based on the strength of a firm’s performance as indicated by their financial statements.
Asset-based lending is also affected by inadequate or unclear financial information. Cassar describes the importance of assets to new business starts and notes that, “due to performance contracting mechanism of banks, several authors suggest that financing will depend upon whether the lending can be secured by tangible assets” (Storey, 1994; Berger and Udell, 1998, Cassar, 2002). To have assets, a business must start, grow and be in the operation stage. Asset lending can be very expensive to monitor for lenders and can be relatively expensive for small business purchases (Berger and Udell, 2002).

Credit scoring and relationship lending are better suited to address the issue of unclear financial information. Credit scoring places heavy weight on the creditworthiness of the owner to gauge the ability to repay loans (Burger and Udell, 2002). The approach is used more often in financing micro-businesses with loan totals of $50,000 or less.

Relationship lending largely bases loan decisions on proprietary information about the firm and its owner gathered through a variety of contacts over time (Ongena and Smith, 2001; Giannetti, 2012). Other information about the firm or owners from suppliers, customers, and community members may also provide lenders with a more general sense of the business environment. “Importantly, the information gathered over time has significant value beyond the firm’s financial statements, collateral, and credit score, helping the relationship lender with informational opacity problems better than potential transaction lenders.” (Burger and Udell, 2002).
Community Banks

Community banks are institutions with less than $1 billion in total assets. “Small businesses consistently appear more willing to ask for credit when their bank is a regional or community bank (and they appear to be more successful in their requests)” (Dennis, 2012). Community or small banks’ greater reliance on relationship lending can help address some issues associated with lack of clear information, which may lead to higher rates of lending. According to Berger and Udell (2002), “a small bank may be able to resolve some contracting problems associated with the relationship lending by eliminating layers of management and reducing the agency problems between the loan officer and senior management”.

FDIC Call reports, based on deposits, illustrate the significant presence of community banks in the SOI (Figure D1). Of all depository institutions in the SOI region, community banks are the most common type of institution. Decreases in total assets from 2007 to 2011 did not change the fact that small community banks represented the largest number of institutions and principal lending source for small business loans.
While community banks with assets under $1 billion represent less than 11% of banking assets, they provide nearly 40% of loans by the banking industry to small business, extending credit that is crucial to job creation. They have a unique role to play in our financial system, (FDIC, 2007). Compared with larger counterparts, community banks in the SOI issued a significantly higher portion of their loans to small businesses (Figure D2) (FDIC, 2011).
The FDIC in January, 2011 convened a forum on “Overcoming Obstacles to Small Business Lending.” Congressman Spencer Bachus, Chairman of the House Financial Services Committee, recognized the importance of community banks in his opening remarks:

... while failures peaked in 2010, the FDIC’s losses were down because smaller institutions were failing. The fact that smaller community banks are failing can be partially traced back to government policies that gave our too-big-to-fail institutions, in my opinion, a competitive advantage. The fact that community banks are failing will have disastrous impact on small businesses going forward because these small banks are more likely to extend credit to small businesses than their big bank counterparts. (FDIC, 2010)

FDIC Acting Chairman Martin Gruenberg noted the importance of community banks in his address to the American Bankers Association Annual meeting on October 25, 2011 when he stated, “the FDIC is going to undertake a number of initiatives to further our understanding of the challenges and opportunities for community banks and to convey the importance of community banks to the FDIC’s mission.” (Gruenberg, 2011).
presence of community banks in the SOI presents an opportunity for economic development practitioners and bank representatives to collaborate and better meet the needs of small businesses with further growth in the region. An important role may remain for a community bank that has an advantage over large banks in extending loans to small businesses. Their local roots and knowledge of the local community and the entrepreneurs who run local businesses may be critical in providing the type of relationship-driven loans that many small businesses need.

**Small Business Administration**

Commercial banks may hesitate to lend to business startups even though the Small Business Administration provides loan enhancements and grants to encourage capital access for small businesses. The SBA 7a and 504 loan enhancement programs are available to banks to help reduce the risks that may otherwise prohibit them from lending to small firms in their early stages.

In addition to banks, the SBA provides access to loan enhancement programs to credit unions, community development financial institutions (CDFI’s), and community development corporations (CDCs). “Surprisingly, small firms do not finance their investment significantly more from government sources or development banks despite the fact that such programs are often politically justified as increasing financing for small firms” (Beck, et al., 2003).

CDFI’s offer microloans, financial services and business training to entrepreneurs and underprivileged populations. The organizations provides lending services, often backed by SBA loan enhancements based on financial status of applicant and offers tailored made repayment plans to meet the requirements of customers. CDFIs can help underprivileged
and rural communities by offering savings as well as credit programs that teach money management skills. Apart from conventional loan programs, CDFIs provide several insurance plans, which help meet financial losses caused by fire or natural disasters.

An analysis of traditional capital activities by FDIC recognized institutions and SBA backed loan activity in the SOI illustrates the impacts of the SBA products. Based on SBA information regarding 7a and 504 loans in the SOI and the FDIC reported activity, loans in the SOI increased each year from 2008 to 2010 despite adverse economic conditions (SBA, 2011; FDIC, 2011). Total SBA approved loans increased and the amounts lent increased also.

Figure D3: SBA 7a & 504 - New Jobs vs. Total Loans in SOI Region

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>7A Loans</td>
<td>187</td>
<td>169</td>
<td>207</td>
</tr>
<tr>
<td>504 Loans</td>
<td>28</td>
<td>18</td>
<td>30</td>
</tr>
<tr>
<td>7A Jobs</td>
<td>402</td>
<td>537</td>
<td>820</td>
</tr>
<tr>
<td>504 Jobs</td>
<td>239</td>
<td>158</td>
<td>279</td>
</tr>
</tbody>
</table>

Higher lending meant more jobs created and retained. (Table D3). While total loans, loan amounts, and jobs increased in the SOI, the average loan amount was substantially lower than in the combined state averages. According to SBA reports, SOI banks issued a total of $91,895,433 in 7a and 504 backed loans in 2010 with an average of $387,744 per loan, compared to a combined state average of $821,661 (SBA, 2011) making increased
access to SBA loans in the SOI an important consideration for both access to capital and job creation.

Table D3: Jobs Created & Retained by SBA 7a Loan Size in SOI

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Employees Per Loan</td>
<td>1.2</td>
<td>2.6</td>
<td>2.9</td>
</tr>
<tr>
<td>Retained Employees Per Loan</td>
<td>3.2</td>
<td>6.3</td>
<td>3.5</td>
</tr>
<tr>
<td>SOI 7A Average Loan Amount</td>
<td>$86,148</td>
<td>$117,817</td>
<td>$176,334</td>
</tr>
</tbody>
</table>

SBA programs resulted in an increase of small business loans and jobs created, but preliminary findings from Illinois respondents of the SOI Small Business Capital Access Survey suggest that more improvements are needed. More than one-third (36%) reported no use of the 7a program and slightly more than one-half (56%) made only 1 to 10 loans in the past 12 months. Illinois bankers reported the need for improvements in the SBA programs including higher guarantees, less paperwork in making loans, and elimination of fees. While SBA programs may need improvements based on the survey, they have been effective in providing capital to SOI small businesses.

Supported Debt Finance

Additional sources of debt financing are available from a variety of government assisted and/or not-for-profit financial entities that provide diverse low interest loan programs to meet a wide range of small business start-up needs. At the national, state, and even local levels, there are programs focused on encouraging small business growth. These programs are usually low interest loans, often backed by federal programs or grants. Community Development Financial Institutions (CDFI) and revolving loan funds (RLF) are two common tools used at the municipal or county level to support business development directly. Both government and non-governmental organizations provide minority groups or target
industries such as technology innovation with designated funding in response to identified needs in the region.

Based on discussions in a focus group meeting with financial institution representatives in the Rockford area, creating a more complete financial delivery system with better coordinated programs is an important opportunity in the SOI. The region has access to several programs most of which provide ways to absorb risk and increase capital to grow small businesses. Compiling and spreading more information about these programs within the SBDCs, incubators, accelerators, economic development organizations and other service providers, including banks, would increase opportunities for funding additional business ventures.

**Trade Credit**

Trade credit is “a critical source of finance for many small businesses but is often ignored when assessing credit availability, and one that can be interchanged with credit from financial institutions” (Dennis, 2012). Trade credit occurs when one business delivers a good or service to another business with an agreement to be paid later. Effectively, the seller loans money to a buyer by not requiring cash at the time of delivery. Trade credit terms remain economical if negotiated and monitored carefully to limit the cost of credit.

Unlike bank loans, trade credit is expected to be repaid within days or weeks. “Forty-seven (47) percent of small-business owners acknowledge using trade credit; 46 percent do not, and 7 percent do not know (Q#21). The 7 percent no answers are likely light or non-users” (Dennis, 2012, p. 37). Results of recent surveys show that those using the most trade credit have had to increase lines of credit and loans due to tightening of trade credit. The tightening is likely to reflect strain from lack of payment.
Trade credit is especially important to businesses lacking access to bank capital. During recessions, businesses seek trade credit when bank financing may be unavailable (Love et al., 2007). Businesses may find their product suppliers more willing to extend credit than formal financial institutions because suppliers have more complete information about businesses than banks (Burkart & Ellingsen, 2004). Trade credit also provides a means for large, credit-worthy supplying businesses to pass their financial access through to smaller purchasers (Boissay & Gropp, 2007) and large suppliers often provide discounts for early payment in order to reduce the risks of lending (Klapper et al., 2011).

**Microfinance**

Microfinance agencies provide financial services to populations, such as those in poverty, without access to typical banking services (Hoje et al., 2009). Started as a movement towards social responsibility to eliminate poverty in developing countries, microloan programs have been adapted in the US and enable individuals to start businesses without access to traditional bank capital. Microloans are made in small amounts with high interest rates over a short term (Hoje et al., 2009). Most of the entrepreneurs receiving microloans will not become large employers in the region but, nevertheless, can employ several workers which is important in small rural economies.

Microfinancing organizations represent a small fraction of the US financial market but their total loans increased 68 percent between 2002 and 2008 (Klein, 2010). Small business microloans averaged approximately $9,000, with a maximum amount of $35,000. When the supply of traditional bank loans for small businesses decreased, microfinancing organizations increased their lending activity (Klein, 2010).
Different approaches to offering microloans exist, including person-to-person as well as a security or note from a microfinance institution that creates the fund. For an example of person-to-person microlending, www.Prosper.com allows individuals to list their needs for loans between $2,000 and $25,000 and investors provide loans at interest rates contingent on a measure of investment risk calculated by the website.

Non-profit organizations often act as intermediaries between acquiring the investment and providing the loan. Two large US-based online microfinance institutions are MicroPlace (https://www.microplace.com) and Kiva (www.kiva.org) both of which provide online networks connecting borrowers and investors (Hoje, et al., 2009).

Maine has been especially active in working with the Small Business Administration using programs such as Incubators Without Walls (www.whecacap.org/index.php). These programs are designed to provide low cost or free training programs for entrepreneurs and individuals interested in launching a business venture. A related example is MaineStream Finance (mainestreamfinance.org) which operates as a Community Development Financial Institution.
Appendix E: Small Business Equity Options

Crowdfunding

A relatively recent funding alternative that is growing in popularity for small businesses and microenterprises as an equity approach is crowdfunding - the process of raising money from a group of people. Crowdfunding models include those for financial return (equity and lending) as well as for projects that appeal to the personal belief of the funder (donation and reward). Crowdfunding expands the “friends and family” stage, adding investment from people unknown to the entrepreneur.

While ‘donation and reward’ crowdfunding has gone on in the past in the US, equity and lending crowdfunding will expand in 2013. The Crowdfunding Act, signed as a component of the Jumpstart Our Business Startups (JOBS) Act signed on April 5, 2012 by President Obama has opened opportunities for entrepreneurs and business starts by removing regulatory barriers to raising capital from investors. The amended rules allow entrepreneurs and new ventures to solicit funding with limited Security and Exchange Commission (SEC) filings, and with limited opportunities to advertise and promote the offering (Anthony, 2012).

Those seeking funding through crowdfunding must file with the SEC and include information similar to what a bank would require for a loan (Anthony, 2012):

- Names and contact information for owners, directors, and officers;
- Business plan of the issuer;
- Financial statements and/or income tax returns
  - For offerings of $100,000 or less, a certification by the principal executive that the financials are correct
  - For offerings between $100,000 and $500,000, financials must be reviewed by a CPA
For offerings above $500,000, financials must be audited

- A description of intended use of the funds;
- A description of the value (including future valuation methods) of crowdfunded shares, rights of crowdfunded shareholders, and how these values and rights; might be affected by other ownership/capital structure of the firm; and
- Other risk factors.

Equity and lending crowdfunding platforms allow companies to sell shares, up to $1 million to any investor in a 12-month period. The annual income of the company is the basis for the allowable amount of investments. For those investors with less than $100,000 annual income or net worth, their investment limit is the greater of $2,000 or 5% of their net worth or annual income. For investors with more than $100,000 annual income or net worth, the allowable amount for investment is up to 10% of the investor’s annual income, not to exceed $100,000 (Rotblut, 2009).

The National Crowdfunding Association (NLCFA) (2012) was formed prior the JOBS Act, with a mission to support, promote, and educate the crowdfunding market. Services include or will include networking and collaboration, group growth, support, operations and deal management, professional development and industry trends as well as public policy involvement that support and promote crowdfunding. While crowdfunding is relatively recent, it opens entrepreneurs to a much broad range of funding support.

Angel Investors

Angel investors use their wealth to invest in a new business opportunity at the earliest stages in return for a stake in ownership. These investments come in the form of convertible debt or preferred stock. Interest in companies that will provide a large gain when sold or going public is preferred over “lifestyle” companies that have limited earnings
potential, including local restaurants, retail shops or small consulting firms (DeBaise, 2010). Angel investors accredited by the Securities and Exchange Commission provide entrepreneurs with the assurance of investing long-term; unaccredited investors can withdraw investment at any time resulting in financial distress of the new business (Gaebler.com, n.d.)

Angel investors are usually interested in seeding start-up companies, often in industries where members have experience. Aside from financial support, angels invest by providing time and expertise to help them succeed. Much, if not most, of the angel investment occurs in major metropolitan areas but, depending on where the investors are located, can occur in rural areas as well. The tasks associated with finding worthy investments require deal sourcing, reading business plans, conducting due diligence, engaging legal support, and monitoring investments to determine follow-on or exit strategies, all of which can be time-consuming and expensive (Mercil, 2006).

Priorities for Angel Investors

When considering investment opportunities, 25 priorities for angel investors were studied by Sudek (2006; 2007) and the findings show four top priorities: 1) trustworthiness and honesty of an entrepreneur, 2) the management team, 3) enthusiasm / commitment of the entrepreneur, and 4) potential exit routes (potential liquidity).

The lowest priorities for angel investors are 25) opportunity for involvement in the company, 24) alignment of investor’s expertise with gaps in the business, 23) ability to reach break-even without further investing, and 22) size of investment. Business angels’ investment emphasis is closer to Venture Capital Fund Managers than banks. Wiltbank (2005) applied the Venture Capital model of investment variables to angel investing
practices to evaluate how the variables affect angel investor outcomes. The model could not consider other variables that are important to angel investors such as management talent and execution processes. Based on the comparisons, angel investors experience fewer negative exits when investing in the earlier stage of the business life cycle since this stage fits the angel investors’ expertise. More post-investment participation also relates to fewer negative exits. The median of negative exits occurred at 3.5 years while the median time for successful exits is 5.8 years.

However, since angels are individual funders, emphasis is on suitability with personal investment criteria. This restricts an angel’s investment consideration to those industries and markets for which he or she has some prior knowledge so as to minimize risk with the investment decision. Business angel investors seek personal satisfaction from their investments and thus entrepreneurs may have to appeal to angel investors on an emotional level.

**Angel Investment Trends**

The Center for Venture Research conducts national research on equity financing by angel investors for early stage entrepreneurial ventures. During the past ten years, the total number of entrepreneurs funded by angel investors increased 54.3%; active investors increased 62.7% and total investment dollars increased 69.7% (Table E1). The impact of the Great Recession during the years 2007-2009 is shown by a decrease in investment dollars from the previous year. In the two most recent years for which data are available (2010-2011) total investment dollars had returned to 2004 levels.
Table E1: Angel Investments for New Enterprises 2002-2011

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Entrepreneurs</th>
<th>Active Investors</th>
<th>Total investment ($B)</th>
<th>Increase / Decrease over prior year</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>66,230</td>
<td>318,480</td>
<td>$22.5</td>
<td>12.10%</td>
</tr>
<tr>
<td>2010</td>
<td>61,900</td>
<td>265,400</td>
<td>$20.1</td>
<td>14.00%</td>
</tr>
<tr>
<td>2009</td>
<td>57,225</td>
<td>259,480</td>
<td>$17.6</td>
<td>-8.30%</td>
</tr>
<tr>
<td>2008</td>
<td>55,480</td>
<td>260,500</td>
<td>$19.2</td>
<td>-26.20%</td>
</tr>
<tr>
<td>2007</td>
<td>57,120</td>
<td>258,200</td>
<td>$26.0</td>
<td>1.80%</td>
</tr>
<tr>
<td>2006</td>
<td>51,000</td>
<td>234,000</td>
<td>$25.6</td>
<td>10.80%</td>
</tr>
<tr>
<td>2005</td>
<td>49,500</td>
<td>227,000</td>
<td>$23.1</td>
<td>2.70%</td>
</tr>
<tr>
<td>2004</td>
<td>48,000</td>
<td>225,000</td>
<td>$22.5</td>
<td>1.24%</td>
</tr>
<tr>
<td>2003</td>
<td>42,000</td>
<td>220,000</td>
<td>$18.1</td>
<td>14.00%</td>
</tr>
<tr>
<td>2002</td>
<td>36,000</td>
<td>200,000</td>
<td>$15.7</td>
<td>-47.70%</td>
</tr>
</tbody>
</table>

Source: Center for Venture Research, 2003; (Sohl, 2004-2012).


At the depths of the recession, in 2009 and 2010, angel investors shifted their focus away from startups and a majority of total angel investment went to established, post-seed businesses. In 2011, the percentage of total angel investment going to post-seed businesses decreased as the share of investment in startups increased. This suggests that angel investors have begun redirecting their attention to new businesses as the economy improved. Although the majority of total angel investment in the recession was in established businesses, the movement away from supporting startups appears to be a result of the business cycle rather than a new, long-term trend.
Figure E1: Startup vs. Post Seed Investing Trends, 2007-2011


Angel investors exit more frequently via mergers and acquisitions than through bankruptcies which may be because of the greater expertise of investors and some involvement in management decisions. In the most recent year for which data are available (2011), the figures show both exits are at their lowest points over the past five years which might be unexpected during a weak economic recovery (Figure E2).

Figure E2: Angel Exit Trends, 2007-2011

Finding Angel Investors

Access to angel investors is not limited to local individuals, resources, or groups. More recently, angel investors have created organizations that formalize equity financing for entrepreneurs. The Kauffman Foundation provided seed funding to support the creation of these organizations. Experienced leaders in the Angel Capital Association are assembling best practices in starting and operating a network of angel investors, developing dissemination vehicles for this information as well as quantifying angel investor organizations and operations (Payne, n.d.). This additional information should facilitate connections between entrepreneurs and potential angel funding opportunities.

Gust

Gust is a computer software platform for managing deal flows used by more than 750 angel groups, venture funds and other investment organizations worldwide. (Angel Capital Association, 2012). Entrepreneurs use Gust tools to facilitate the processes of funding and sponsoring new business startups. According to the Gust website, (www.gust.com) more than 50,000 applications for funding support from entrepreneurs in 34 industries were received during the past 12 months, indicating the volume and appeal of this approach and more than 35,000 affiliated investors used this platform. Investors can browse business reviews and gauge interest on a secure and private platform. Message boards keep all deal information in one central location so that file sharing of business plans and financials on Gust can occur. Applicants provide a one-page overview for easy business comparisons. Email, web or customizable applications can match the deal flow process (Gust, 2012).
**RAIN Source Capital**

RAIN Source Capital (2011) organizes angel investors who have interest in supporting growing companies. RAIN Source forms individual funds, adds other capital, and shares expertise from among and between funds that they manage. An average investment from angels averages between $25,000 and $100,000 in a fund and it is member-led with a specific industry focus for the fund. Usually companies that already have raised capital, including friends and family resources, and with the potential in five years to be a $10 million company are considered.

RAIN funds can benefit smaller communities that are not targets for other equity resources. RAIN Source Capital creates sustainable investment funds, along with providing expertise to grow businesses that create jobs and build local wealth as well as recruit and foster companies paying high wages. As of 2011, RAIN currently had eight investment funds that meet actively with entrepreneurs (RAIN Source Capital, 2011). Four of these funds were in Minnesota and the others were in Idaho, Montana, and South Dakota.

**Cimarron Capital Partners**

Another approach to enhancing investment activity in a region while maintaining a competitive return on investment is possible through the “fund of funds” model developed by Cimarron Capital Partners (Cimarron Capital Partners, 2012). Under the “fund of funds” model, a regional investor such as a state government invests money in multiple venture capital funds with the intent of promoting economic development while receiving a return on previously idle cash. With interest in seed to early stage business funding, Cimarron Capital Partners work with states or regions to develop funding in support of the entrepreneurial ecosystem and attracting investment. Clients include the Arkansas Institutional Fund, Iowa Fund of Funds and Oklahoma Capital Investment Board.
The Iowa Fund of Funds invests in seven private venture capital funds specialized in industries such as manufacturing, consumer services, health care, and education (Iowa Capital Investment Corporation, 2013). The Arkansas Institutional Fund has a portfolio including mainly venture capital funds that either support an Arkansas business or are based in the state (Arkansas Venture Capital Investment Trust, 2012). The Oklahoma Capital Investment Board has a portfolio of 19 venture capital funds including 16 firms with an office located in the state (Oklahoma Capital Investment Board, 2013).

**Venture Capital**

A venture capitalist is a professional investor with interest in building early, innovative businesses and actively working with the entrepreneurial management team. Venture capital investors manage an investment fund raised from institutional investors such as pension funds, insurance companies, endowments, and foundations. As managers of the fund, venture capital investors are “general partners” having responsibility to the “limited partners” those who invest the money. The venture capital fund manager, with the trust and confidence of limited partners, manages and protects the limited partners’ money, when making investments of at least $5 million in new businesses.

In 2010, the United States had 462 active venture capital firms, down 55% since the height of the technology bubble in 2000 (National Venture Capital Association, 2012). Venture capital fund investors typically expect repayment within 3 to 7 years through either buy-out by another company or going public and selling shares through an initial public offering (FundingPost.com, n.d.).

**Priorities for Venture Capital Investment**

Venture capitalists expect a higher rate of return than traditional investors, typically 25% or more (Ward, n.d.). Early stage businesses have difficulty attracting venture capital
without a reasonable cash flow, which usually occurs in Stage 2: Early growth. Early stages make predicting success more difficult due to the instability of the business, unknown markets and lack of record of accomplishment (Grupp & Sapienza, 1992 in Wiltbank, 2005).

Venture capital (VC) funds can specialize according to the life cycle stage; however, avoiding seed stage\(^7\) funding is typical of many venture capital organizations (Figure E4). According to information from Thomson Reuters, in 2011, the venture capital funds were split by approximately one-third in early stage, expansion, and later stage.

Figure E3: Venture Capital Investment by Stage, 2011


Venture capital fund managers (VCFM) place high importance on the ability of the management team, including their skill, quality, characteristics and record of

\(^7\) Thomson Reuters stage definitions varied slightly from the description provided within this document. Thomas Reuters’s Seed is equivalent to Stage 0: Pre-venture; early stage is equivalent to Stages 1 & 2: Existence/infancy and Early Growth.
accomplishment. Market/industry characteristics, environmental threats, competition levels and product differentiation are also considered. VCFMs are driven by returns on investment as they manage funds for outside investors.

McMillan, et al., (1985) studied criteria used to evaluate investment opportunities by venture capitalists including 27 criteria organized into six major groups. Top priorities included: 1) personality and experience of the entrepreneur, especially evidence of staying power and ability to handle risk; 2) product and market characteristics, including proprietary protection\(^8\) for the product and high growth rate as the most appealing market characteristic; and 3) financial considerations, especially high upside potential and high investment liquidity, although a 10 year payout rather than five years was likely.

McMillan et al., (1985) also reported that 84% of venture capitalists would disqualify a venture from investment if the entrepreneur lacked evidence of staying power and a potential for a 10 times return on investment within 10 years. The criterion of concern in every case of critically flawed ventures is the entrepreneur’s personality or experience. The business plan had to indicate as clearly as possible the staying power of the entrepreneur, a record of accomplishment, ability to react well to risk and target market familiarity. The ability to pull together a team as well as to demonstrate leadership of the team is a critical capability of the entrepreneur for venture capitalists.

**Venture Capital Investment Trends**

The National Venture Capital Association (NVCA) is the venture community’s trade association that accumulates and disseminates statistics regarding the venture capital industry. Prior to 2009, reports on the number of deals and total investments were

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\(^8\) Although claiming “high tech” was not important, 70% of all ventures are in the “high tech” category.
available only at the broad regional level but state level data have been available since 2009 (Thomson Reuters, 2012). State data for Illinois and Wisconsin between 2009 and 2012:3Q show that 2012 activity decreased from 2011 and, in Wisconsin, had not returned to the 2009 level (Figure E5).

Figure E4: Total Venture Capital Deals in Illinois & Wisconsin, 2009 – 2012 3Q

![Graph showing venture capital deals in Illinois and Wisconsin from 2009 to 2012.](image)


The average amount of venture capital invested for each deal in Illinois and Wisconsin was less in each year compared to the US, except in 2010 when Illinois exceeded the US average by $3 million per deal. In 2010, both Illinois and Wisconsin increased in venture capital investments by 111% and 177% respectively (Figure E6).
Investor’s Circle

Investor’s Circle members include high net worth individuals, venture capitalists, investment advisors, family office managers, and foundation officers. They pay an annual fee, providing for facilitation of capital flow from investors to private, early stage, for profit companies and small venture funds plus invitations to participate in Venture Fairs.

Venture Fairs allow entrepreneurs to pitch companies positioned for regional or national growth and committed to environmental and social improvements. Among preferred industry sectors obtaining support from Investor’s Circle are Cleantech (Energy & Environmental Solutions), Community & Economic Development, Healthcare, Biotech & Wellness, Sustainable Consumer Products, and Digital Media, Software & Education.

Virtual Venture Fairs are conducted monthly using webinars to allow more frequent entrepreneur pitches. Semiannual Venture Fairs occur in the fall (on the East Coast) and spring (on the West Coast), usually over two days. The schedule includes meetings,
networking and working sessions along with the key focus of the Fair: the companies’ business presentations. Deal-making results during the final day of the event.

Entrepreneurs submit an application along with a fee to be considered for investment. Applications including specific criteria are submitted on a rolling basis. To qualify, a business must be fully-formed with one year experience and expected to achieve $5 million or more in revenues in the next five years. Gust is the on-line deal database for investors to review and research the opportunity. Investor Circle staff review all applications within four weeks of submission to determine whether they can advance in the process. Applications can be for either virtual or semi-annual Venture Fairs.

Next, review committees consisting of Investor Circle members are formed to select applicants to present their business ideas to potential investors. One month prior to the Venture Fair, an entrepreneur receives assistance in preparing the presentation and other supporting materials. The review committee evaluates the presentations prior to the event.

Revenue-based Financing

Often dubbed "royalty-based financing", revenue-based financing is used by the film and natural resources industries—paying investors a percentage of gross receipts. This approach allows entrepreneurs to focus on growing their businesses with flexible repayment schedules and without loss of control. Both equity and traditional debt financing structures are used to meet capital needs of expanding businesses. A lump sum for unrestricted growth and no obligation to repay in the event of insufficient future revenues, in exchange for a percentage of future revenues, is the basis for structuring the
Interest rates are higher for revenue-based financing agreements than for traditional bank loans as investors expect a return 3 times the capital provided based on a simple or time-adjusted percentage and may incorporate a rate of return variable to reflect how much time it takes for repayment. This approach is best suited for early-stage companies with more risk than traditional banking will accept while having less risk and upside than expected by risk capital investors.

Revenue-based financing works best for businesses that generate sales with well-defined capital requirements and limited scaling potential. Their need is for additional capital to take full potential of opportunities and grow as fast as possible (Morell, 2012; Jones, 2012). Lighter Capital and Royalty Capital New England are examples of investment funds that create revenue-share finance deals for entrepreneurs.

**Lighter Capital**

Lighter Capital offers loans to businesses ranging from $25,000 to $500,000 in proportion to the business’ annual revenues. The loans are repaid monthly as a percentage of the business’ total revenue so the borrower’s total payment decreases in months where revenues decrease (Lighter Capital 2011).

Loans from Lighter Capital are retired when borrowers repay a total amount determined when the loan is made, with most loans having a term of one to five years. The loans are designed primarily for businesses in technology or knowledge-based industries and they are not offered for startups. Lighter Capital encourages businesses in asset-intensive industries such as manufacturing, construction, and food service to seek capital
from traditional sources instead of Lighter Capital because they can offer collateral (Lighter Capital, 2011).

Lighter Capital seeks businesses with at least $200,000 in annual revenues and interested entrepreneurs may apply on-line. As of 2011, the company has invested in 17 businesses nationwide with most providing software or web-based services. Lighter Capital is not currently invested in any companies within the SOI region and the only Midwest-based company receiving investment was a Minnesota software developer for nonprofit organizations (Lighter Capital, 2011).

**Royalty Capital New England**

Royalty Capital New England is an investment fund offering revenue-based financing to businesses with established presences in their industries, existing revenue streams, and potential for rapid growth. The principal amount is negotiated between business owner and investor and investors receive a return on investment that is a multiple of the principal. Each month the borrower pays a fixed percentage of its total revenue, repaying the loan’s principal within 48 months and then paying the investor’s return within four to six years. Royalty Capital New England states that borrowers benefit from reduced capital costs due to interest deductibility and that it requires no commitment of personal assets and (Royalty Capital New England, 2011).

**Community Supported Enterprises**

The Community Supported Enterprise (CSE) functions similarly to the Community Supported Agriculture (CSA) model. CSA brings a community of individuals together, pledging support to a farming operation by signing up to receive a weekly delivery of farm
products. The farmers receive the capital needed to maintain and grow their crops and members receive their share of food throughout the growing season.

With difficulty in finding capital without losing control of the company once the business is up and running, individuals can establish a relationship with a growing business by purchasing coupons from the company that are redeemable at stores for the product. This provides the business with necessary upfront capital, helping to ensure long-term viability.

Most often, the CSE supports and preserves local communities, through a combination of charitable and investment contributions, particularly when the community commits to supporting the new startup. A Memorandum of Understanding reinforces the partnership between the new business and the community, outlining the arrangement’s spirit and principles as well as circumvents misunderstandings. Details of CSE arrangements and examples of implementation are evident in The Preservation Trust of Vermont.

The Preservation Trust of Vermont promotes numerous CSEs within the state of Vermont. One example includes a local restaurant that avoided closure by collecting $1,000 contributions from customers that were repaid via quarterly $90 coupons for the restaurant. Another restaurant collected $5,000 each from 32 investors and repaid them in savings of 25% on all meal purchases at the restaurant for five years. Vermont’s CSEs also include a general store where customers may pay $15 annually to receive discounts on all purchases (Preservation Trust of Vermont, n.d.). As shown by these examples, CSE arrangements are scalable for the business’ capital needs and preferred repayment schedule.
Appendix F: Local Loan Funds in the SOI Region

City of Evansville Revolving Loan Fund

**Purpose**

The RLF is designed to facilitate business development projects within the City of Evansville that create investment and employment opportunities.

**Eligibility**

Any CEO, or an equivalent, seeking to establish a new operation, expand an existing or start-up a new business in the Evansville area, may submit an application.

Loans *cannot* be used for debt financing, residential projects (unless directly related to business conversion), studies or other “soft” costs, maintenance, or involuntary relocation payments. Nor can funds be used to finance any of the following businesses: speculative investment and/or real estate investments, non-profit business or organizations, lending institutions, gambling operations, and non-public recreation facilities.

The following activities are eligible for program funds: land, building, and fixed equipment acquisition; site preparation and construction, including site clearance, demolition, removal or rehabilitation and improvements; the reconstruction or installation of buildings and fixed equipment; the payment of assessments for sewer, water, street, and other public utilities if the provision of the facilities will directly create/retain jobs; working capital, including marketing; workforce development and/or training.

**Requirements**

To be eligible for funding, all of the following minimum conditions will be considered:

1. A minimum of $1 of private funds leveraged for every $1 of loan funds requested;

2. The creation/retention of at least [1] full-time equivalent, permanent position - excluding those filled by owners/partners or family members - for every $10,000 dollars requested;

3. Project viability and ability to repay the loan;

4. Compliance with all applicable local, state, federal codes and laws; and

5. Project completion within 36-months of loan approval, detailing hiring, construction, and other relevant time-bound schedules.

6. Inability to obtain adequate funding from other sources.

**Conditions**

Applications may be submitted at any time during the year. All completed applications are subject to review by Evansville Economic Development Committee and the RLF Review Board. The City’s Common Council determines all final loan decisions.
Loan amounts are subject to program fund availability and eligibility criteria. Terms are as follows (maximum terms listed): working capital - 5 yrs.; machinery, equipment and fixtures - 7 yrs.; and real estate - 10 yrs. Rates are between 4% and prime. To secure 100% of the loan, assets to be purchased with loan proceeds and any/all other assets owned and/or used in the business, plus personal guarantees are required. No funds will be released without written commitments from other funding sources.

Repayment schedules are monthly; interest and/or principal may be deferred for up to two (2) years, depending on recommendations of the said review. Interest shall accrue during this deferment period, and be added to the principal loan amount. Thereafter, both interest and principal shall be collected for the remaining term of the loan to maturity. No loan shall be subject to any penalty for prepayment prior to the term of the project. However, late payment penalties are applicable.

Failure to comply with any of the provisions of the RLF may result in default. In addition to the said requirements in the Loan Recipient Obligations section, the following shall also be considered as a default:

1. Recipient’s failure to create / retain the specified number of jobs within a specified time frame;
2. Failure to make any payment of interest or principal within 30 days after payment due date;
3. Defaulting on other loans with private lenders;
4. Cessation of operations or movement of business from the City;
5. Sale of the business.

In the event of default, the City will issue a Notice of Default. All relevant and interested parties, including but not limited to other secured lenders, will be notified of default. Once issued, all sums due and owing the City shall, at the City’s option, become immediately due and payable. To avoid foreclosure and any other collective actions, the default must be cured not less than 60 days from the date of notice.

Janesville Gap Funding TIF Loan Program

This program is designed to provide loan funding to help companies have increased access to capital for expansion purposes. The purpose is to assist in the financing of job-creating expansion projects which cannot be adequately financed using only private sector and equity funding. Without the TIF loan filling the remaining financing gap, the project would not go forward.

Gap loans are to be made to for-profit businesses located in specified TIF areas within the City of Janesville. Loans may be made for business start-up, expansion or for business recruitment. Businesses will need to commit to retention or expansion of jobs to receive funding.

Desirable businesses

1. Manufacturing/Assembly
2. Warehouse Distribution
3. Professional services including computers, phones and other technology-related product or service-oriented companies

*Eligible uses of funds*

1. Purchase, expansion or remodeling of commercial real estate
2. Purchase of machinery and equipment
3. Working Capital

*Ineligible uses of funds*

1. Loans where primary repayment source is future equity or potential refinancing of debt
2. Loans without a secondary source of repayment
3. Loans for political purposes
4. Loans for speculative purposes
5. Loans secured by restricted stock in closely-held corporations

*All TIF loans will be secured via subordinated lien interest.*

All loans require personal guarantees of the owners which have 20% or greater equity in the business. All TIF loans to be term loans. No revolving credit lines.

All TIF loans require a minimum of annual payments. The subordinated “TIF” portions of the loans will match the lender’s market rate terms and interest but at no time will the term exceed 10 years. Subordinated loans to be priced at fixed market rates to be determined at the time of the loan request. Typical size of TIF “gap” loan - $20,000 to $50,000 based on the expansion project.

*City of Beloit Commercial and Industrial Revolving Loan Program*

*Objectives*

1. Stimulate private sector investment into long-lived physical plant and equipment to increase productivity and create new employment opportunities, including opportunities for Low and Moderate Income (LMI) persons.
2. Provide financing to fill gaps in local capital markets and thereby stimulate private sector capital formation, and to serve as a “pump primer” rather than a replacement for private commercial lending.
3. Aid small business, especially those that have a high multiplier effect on jobs and income.
4. Stabilize and diversify the City's economic base.
5. Foster the retention and expansion of financially and managerially sound existing industries.
6. Attract financially and managerially sound new industries and capital to the City.
7. Support start-up businesses in the City.
**Eligible Area**

The activity financed and its benefit must be within the municipal boundaries of the City.

**Eligible Applicants**

Eligible applicants are for-profit commercial, industrial or service sector businesses who will locate or expand in the City by creating new jobs, of which more than 51% must be LMI people at the time they enter the job or enter the job training. Businesses that will retain jobs that would have otherwise moved out of the City are also eligible, if more than 51% of the jobs retained are for LMI people.

**Eligible Activities**

Program funds shall be used to assist a business to finance exterior and interior building improvements (including upper floor units), purchase of land and building, new construction, purchase of machinery and equipment, land improvements, (i.e., site preparation, sewer and utility extensions, etc.), demolition, and leasehold improvements.

**Ineligible Activities**

Program funds shall generally not be used for working capital; debt refinancing; speculative activities; residential building construction or rehabilitation; routine maintenance of plant or shop facility; specialized equipment that is not essential to business operation; activities complete, begun or contracted for, prior to receiving final approval of an application for funding under this Program; and costs other than those specified in II, D.

**Collateral**

Any available business or personal assets considered adequate and satisfactory to the Corporation.

**Repayment**

Based upon borrower's credit needs, the Program may provide for flexibility in loan repayment to include

1. Delay first payment.
3. Deferrals of principal, or interest and principal repayments for a limited period of time.
4. Extended amortization schedule with balloon payment.

**Walworth County Small Business Revolving Loan Fund**

The Hometown Entrepreneur Loan Program is a small revolving loan fund pool managed by the Walworth County Economic Development Alliance, Inc. It was acquired in 2008 from the United States Department of Agriculture - Rural Development for the use of providing small loans to new and emerging businesses in Walworth County. Under HELP entrepreneurs can secure funds for start-up, business acquisition, and expansion.
**Eligibility**

Must be:

- Located in Walworth County
- Have fewer than 50 employees
- Have gross sales under $1,000,000

**Eligible Use of Funds**

- Real Estate Acquisition
- Equipment Purchases
- Working Capital
- Construction or renovation

**Ineligible Use of Funds**

- Produce agricultural products except for commercial nurseries
- Timber Operations
- Limited agricultural production related to technical assistance projects
- Programs operated by cable television systems
- Funds can only be used for planning given projects and cannot be used for area wide type planning
- Funds may not be used to refinance existing debt

**Types of Financing Available**

- Real Estate
- Equipment & Construction
- Working Capital
- Leveraged Funds

One dollar of private sector investment should be obtained for each dollar of RLF investment. Private sector investment is defined as financing from a private lending institution, public sector business loan programs, other than the Community Development Block Grant program, or new equity that is injected into the business as part of the expansion project. Grants from the Department of Vocational Rehabilitation are not considered eligible matches for loan purposes.

**Equity Requirements**

Borrower must show a minimum of 10% equity in the project being funded.

**Personal Guarantees**

In most cases the Budget & Finance Committee will ask the business owner to sign a personal guarantee.
Loan Terms

The maximum funding available to loan applicants is $50,000, of which matching funds may be required by the loan applicant.

Working capital loans – up to seven (7) years
Machinery, equipment & construction – up to ten (10) years
Real estate – up to twelve (12) years, amortized over 20 years

The interest rate for each loan is set by WCEDA's board of directors and will vary depending upon the borrower’s credit and ability to repay funds.

Fees

All fees are taken off of the top of the loan approval.

$100 non-refundable loan application fee ($100 credit will applied to other fees if loan is approved)
1% loan origination fee
All applicable attorney fees
All title and other collateral security fees

City of Whitewater Economic Development Revolving Loan Fund

Through a grant from the Wisconsin Department of Commerce’s - Community Development Block Grant Program (CDBG), the City of Whitewater has the ability to make loans of varying sizes to businesses that are considering locating within the cities limits.

Loan Programs

Industrial Development Loan Program - This program is targeted to manufacturing, distribution, and related businesses which have greater capital needs and generally provide larger numbers of jobs. Loans made under this program will not exceed $150,000, unless exceptional circumstances merit a greater sum.

Commercial Enterprise Loan Program - This program is designed to appeal to mid-sized to larger commercial and retail businesses. Loans will generally not exceed $50,000 unless exceptional circumstances merit a longer term.

Microloan Program - The intent of this program is to encourage new business formation and expansion of small businesses, particularly those located in the downtown business district. Loans under this program may not exceed $15,000.

Eligibility Requirement

Eligible Area

Projects must be located within the corporate limits of the City of Whitewater in order to be eligible for loans made through the Economic Development Loan Program.
Eligible Applicants

Applications may be submitted by any business wishing to establish a new operation or expand an existing operation located within the City of Whitewater.

Eligible Activities

Program loans are available to applicants for the following activities:

- Acquisition of land, buildings and fixed equipment
- Site preparation and construction or reconstruction of buildings (including leasehold improvements), provided that they are in keeping with any covenants or design guidelines (such as the Whitewater Business Park Covenants) imposed by the City of Whitewater or Whitewater CDA, and are consistent with plans approved by the City of Whitewater Plan & Architectural Review Commission;
- Installation of fixed equipment
- Clearance, demolition, or removal of structures or rehabilitation of buildings (including leasehold improvements) and other such improvements, provided they are in keeping with any covenants or design guidelines (such as the Whitewater Business Park Covenants) by the City of Whitewater or Whitewater CDA, and are consistent with plans approved by the City of Whitewater Plan & Architectural Review Commission;
- Payment of assessments to a business for sanitary sewers, water mains, public streets and other improvements if the provision of the improvements will directly create or retain jobs. The use of Economic Development Loan Program Funds in this manner must be in the form of a loan to a business which is assessed for these costs.

In addition to the above, the Micro-Loan Program may also be used to provide working capital for inventory and direct labor costs only. (This use is available exclusively to Microloan recipients.)

Ineligible Activities

- Refinancing or consolidation of existing debt;
- Reimbursement for expenditures made prior to loan approval;
- Specialized equipment that is not essential to the business operation;
- Residential construction or reconstruction unless such reconstruction is intended to convert the use of the residential building to a business or industrial operation. Program funds may be applied to the exterior or other necessary improvement to mixed-use (commercial/residential) buildings where such improvements are directly attributable to the commercial enterprise operating within the building.

Economic Development Loan Program funds may not be applied to conversion or rehabilitation of residential units.

- Routine Maintenance;
- Professional services such as feasibility and marketing studies, accounting, management services, and similar activities. The cost of legal services incurred in closing the Economic Development Loan Program are eligible;
Façade improvements are not eligible under the Microloan Program.

Other activities that the Loan Review Board may identify during the administration of the program.

**Ineligible Businesses**

Speculative investment companies;
Real estate investment companies (except for facilities from which the business operates);
Lending institutions;
Gambling operations;
Recreational facilities which do not allow access to the general public;
Other businesses not serving the interests of the City of Whitewater;
Any government body or governmental entity (including the City of Whitewater or Whitewater CDA); and
Not-for-profit businesses or organizations.

Businesses are allowed only one outstanding loan under the program.

**Minimum Requirements**

To be eligible for funding, a project must meet all of the following minimum requirements;

Private Funds Leveraged - The applicant must leverage a minimum of one dollar of private funds for every one dollar of loan funds requested. Higher leverage may be required at the discretion of the Loan Review Board.

Cost per Job Created - At least one full time, permanent position must be created for every $20,000 or program funds requested. No part-time jobs will be counted toward meeting this requirement. The CDA may require job creation at a rate greater than one job per $20,000 loaned, upon taking into consideration the type of jobs, hourly wage, benefits, etc.

Financial Feasibility and Business Viability - The applicant must demonstrate that the proposed project is viable and the business will have the economic ability to repay the funds

Low and Moderate Income (LMI) Benefits - The project will provide increased permanent employment or will retain existing jobs which would have been lost locally. Of the jobs created or retained by the project, at least 51 percent must be made available to low or moderate income persons as defined by the US Department of Housing and Urban Development.

Compliance with Applicable Laws. Applicants will comply with all applicable local, state, and federal laws and codes.

Project Completion - Project shall be completed within 24 months from the date of the loan approval.
Owner Equity - Applicants for the Microloan Program must have a minimum ten percent equity in the business to qualify for loan.

Fees

Industrial Development Loan Program - At the time of closing, loan recipients will be assessed a 1% fee for administrative expenses, along with the actual legal fees related to loan origination.

Commercial Enterprise Loan Program - At the time of closing, loan recipients will be assessed a 1% fee for administrative expenses, along with the actual legal fees related to loan origination.

Microloan Program - As the time of closing, loan recipients will be assessed a $150 fee.

City of Elkhorn Economic Development Revolving Loan Fund

Through a grant from the Wisconsin Department of Commerce’s - Community Development Block Grant Program (CDBG), the City of Elkhorn has the ability to make loans of varying sizes to businesses that are considering locating within the cities limits.

Eligible Area

Projects must be located within the corporate limits of the City of Elkhorn in order to be eligible for loans made through the Revolving Loan Fund.

Eligible Applicants

Applications may be submitted by any business wishing to establish a new operation or expand an existing operation located within the City of Elkhorn.

Eligible Activities

Program loans are available to applicants for the following activities:

- Acquisition of land, buildings and fixed equipment
- Site preparation and construction or reconstruction of buildings or installation of fixed equipment
- Clearance, demolition, or removal of structures or rehabilitation of buildings and other such improvements;
- Payment of assessments to a business for sanitary sewers, water mains, public streets and other improvements if the provision of the improvements will directly create or retain jobs;
- Working capital (inventory and direct labor costs).

Ineligible Activities

- Refinancing or consolidation of existing debt;
- Reimbursement for expenditures made prior to loan approval;
- Specialized equipment that is not essential to the business operation;
Residential construction or reconstruction unless such reconstruction is intended to convert the use of the residential building to a business or industrial operation.

Routine Maintenance;

Professional services such as feasibility and marketing studies, accounting, management services, and similar activities. The cost of legal services incurred in closing the RLF are eligible;

Other activities that the Loan Review Board may identify during the administration of the program.

*Ineligible Businesses*

Speculative investment companies;
Real estate investment companies;
Lending institutions;
Gambling operations;
Other businesses not serving the interests of the City of Elkhorn;
Not-for-profit businesses or organizations.

*Minimum Requirements*

To be eligible for funding, a project must meet all of the following minimum requirements;

Private Funds Leveraged - The applicant must leverage a minimum of one dollar of private funds for every one dollar of loan funds requested. Higher leverage may be required at the discretion of the Loan Review Committee.

1. Cost per Job Created - At least one full time, permanent position must be created for every $20,000 or program funds requested. The committee may require a lower job creation rate where warranted, (taking into consideration the type of jobs, hourly wage, benefits, etc.)

2. Financial Feasibility and Business Viability - The applicant must demonstrate that the proposed project is viable and the business will have the economic ability to repay the funds.

3. Low and Moderate Income (LMI) Benefits - The project will provide increased permanent employment or will retain existing jobs which would have been lost locally. Of the jobs created or retained by the project, at least 51 percent must be made available to low or moderate income persons as defined by the US Department of Housing and Urban Development.

4. Compliance with Applicable Laws. Applicants will comply with all applicable local, state, and federal laws and codes.

Project Completion - Project shall be completed within 24 months from the date of the loan approval.
Maximum Loan - The recommended maximum amount to be loaned to any one applicant is limited to twenty (20%) percent of the entire project cost.

**Terms & Conditions**

**Loan Amount**

Loan amounts are subject to the availability of program funds, but are subject to a recommended maximum loan equal to twenty (20%) percent of the entire project cost.

**Interest Rate**

The interest rate shall be established at no less than four percent.

**Terms of Loans**

Working capital loans shall have a maximum term of eight years

Loans for machinery, equipment and fixtures shall have a maximum term of eight years

Real estate loans shall have a maximum term of eight years which can be amortized on a twenty-year basis with the option of refinancing for an additional twelve years upon Loan Review Board approval.

In any case, the loan shall not have a term longer than the terms of the other private financing in the project.

**Village of East Troy Economic Development Revolving Loan Fund**

Through a grant from the Wisconsin Department of Commerce’s - Community Development Block Grant Program (CDBG), the Village of East Troy has the ability to make loans of varying sizes to businesses that are considering locating within the cities limits.

**Eligibility Requirements**

**Eligible Area**

Projects must be located within the corporate limits of the Village of East Troy in order to be eligible for loans made through the Revolving Loan Fund.

**Eligible Applicants**

Applications may be submitted by any business wishing to establish a new operation or expanding an existing operation located within the Village of East Troy.

**Eligible Activities**

Program loans are available to applicants for the following activities:

- Acquisition of land, buildings and fixed equipment
- Site preparation and construction or reconstruction of buildings, including leasehold improvements and façade renovation for commercial and industrial buildings; and/or installation of fixed equipment
- Clearance, demolition, or removal of structures or rehabilitation of buildings and other such improvements;
- Working capital
**Ineligible Activities**

Refinancing or consolidation of existing debt;

Reimbursement for expenditures made prior to loan approval;

Specialized equipment that is not essential to the business operation;

Residential construction or reconstruction unless such reconstruction is intended to convert the building to a business use;

Routine Maintenance;

Professional services such as feasibility and marketing studies, accounting, management services, and similar activities.

Other activities that the Loan Review Board may identify during the administration of the program.

**Ineligible Businesses**

Speculative investment companies;

Real estate investment companies;

Lending institutions;

Gambling operations;

Non-public recreation facilities;

Other businesses not serving the interests of the Village of East Troy;

**Minimum Requirements**

To be eligible for funding, a project must meet all of the following minimum requirements;

Private Funds Leveraged - The applicant must leverage a minimum of one dollar of private funds for every one dollar of loan funds requested. Private sector investment is defined as financing from a private lending institution and cash equity that is contributed to the project by the applicant.

Cost per Job Created - At least one FULL TIME, permanent position must be created for every $20,000 or program funds requested.

Financial Feasibility and Business Viability - The applicant must demonstrate that the proposed project is viable and the business will have the economic ability to repay the funds

Low and Moderate Income (LMI) Benefits - The project will provide increased permanent employment or will retain existing jobs which would have been lost locally. Of the jobs created or retained by the project, at least 51 percent must be made available to low or moderate income persons as defined by the US Department of Housing and Urban Development.

Compliance with Applicable Laws. Applicants will comply with all applicable local, state, and federal laws and codes.
Project Completion - All projects shall be completed, all funds expended, and all jobs created and/or retained within 24 months from the date of the RLF loan approval. All jobs shall be maintained for a minimum of 12 months.

Maximum Loan - The recommended maximum amount to be loaned to any one applicant is limited to twenty (20%) percent of the entire project cost.

Terms & Conditions

Loan Amount

Loans are available from $5,000 to $100,000. Loans exceeding $100,000 shall be looked at case-by-case.

Interest Rate

The interest rate shall be set at the rate currently being offered by the Wisconsin Department of Commerce through its CDBG program. The interest rate shall be fixed for the life of the loan.

Terms of Loans

Machinery & equipment 2-10 years;

Buildings and land - 10 to 20 years and;

Working capital - 1 to 7 years

Geneva Lake Development Corporation- Master Fund (Revolving Loan Fund)

Purpose of the Economic Development Master Fund

The Master Fund has been established to enhance the business climate within the eligible area through the retention and expansion of existing businesses and the development of new, small businesses. Small businesses often lack the necessary capital to develop or expand their operations and this lack of capital has a significant impact on the local economy. The Master Fund program includes funding mechanisms and interest rates that are designed to encourage business development, while providing for the recapitalization and growth of the Master Fund program.

Eligible Applicants

Eligible applicants for the Master Fund are business establishments or property owners located within the eligible area. The exception being building design grants and construction facade loans. This financing is available only within the City of Lake Geneva. Applicants must demonstrate that they are unable to access the financing necessary for the business or real estate project through conventional sources. No GLAD Board of Directors member shall be eligible to participate in the program.

County of Racine Community Development Block Grant Revolving Loan Fund

This program was designed specifically to assist businesses in Racine County. The program primarily finances real estate projects, equipment purchases and limited working capital needs. The CDBG-RLF partners with your bank providing a portion of your financing needs.
Eligible Project Costs
Land and building purchases
Building construction or renovations
Equipment, furniture and fixture purchases
Limited working capital
Demolition, renovation, and improvements of buildings
Purchase of rolling stock

Fees Estimated
$1,000 legal fee
1.5% processing fee
Out-of-pocket closing costs

Rates & Terms
As low as 2%
Up to 5 year term
Up to 20 year amortization
Key man life insurance typically required

County of Racine Economic Development Administration Revolving Loan Fund

This program was designed specifically to assist businesses in Racine County by offering an EDA-RLF loan in partnership with a bank loan. The program primarily finances real estate projects, equipment purchases and limited working capital needs.

The County EDA-RLF offers a below market interest rate, currently as low as 2.44%. Its participation cannot exceed either $200,000 or 33% of the total eligible project costs.

Eligible Project Costs
Land and building purchases
Building construction or renovations
Equipment, furniture and fixture purchases Limited working capital

Fees Estimated
$1,000 legal fee
1.5% processing fee
Out-of-pocket closing costs
Rates & Terms
As low as 2.44%
Up to 10 year term
Up to 20 year amortization
Key man life insurance typically required.

Racine Development Group Revolving Loan Fund

The Racine Development Group (RDG) created a loan fund to promote business development and real estate projects in the City of Racine, with emphasis on low- and moderate- income neighborhoods. Contributing members include Chase Bank, Johnson Bank, M&I Community Development Corp., RCEDC, S.C. Johnson, Tri City National Bank, US Bank and Wells Fargo Bank.

This program partners with bank financing to fund real estate projects, furniture, fixtures and equipment purchases and limited working capital needs.

The RDG offers a below market interest rate, currently as low as 4%. Its participation typically does not exceed either $100,000 or 40% of the total eligible project costs.

Eligible Project Costs
Land and building purchases
Building construction or renovations
Equipment, furniture and fixtures purchases
Limited working capital

Fees Estimated
$1,500 legal fee
1.5% processing fee
Out-of-pocket closing costs
Annual servicing fee of 0.5% collected with monthly payments

Rates & Terms
As low as 4%
Up to 5 year term
Up to 20 year amortization
Key man life insurance typically required.
City of Racine Industrial/Commercial Building Revolving Loan Fund

This program was designed specifically to assist businesses in the City of Racine by offering an I/CB-RLF loan in partnership with a bank loan. The program primarily finances real estate projects where the financing will result in a currently vacant facility in becoming occupied either by the borrowing business or a tenant.

The City I/CB-RLF offers a below market interest rate, currently as low as 2.44%. Its participation cannot exceed either $200,000 or 33% of the total eligible project costs.

*Eligible Project Costs*
- Land and building purchases
- Building construction or renovations
- Loans to developers where the building will become tenant occupied
- Environmental remediation

*Fees Estimated*
- $1,000 legal fee
- 1.5% processing fee
- Out-of-pocket closing costs

*Rates & Terms*
- As low as 2.44%
- Up to 10 year term
- Up to 20 year amortization
- Key man life insurance typically required.

City of Racine Brownfield Cleanup Revolving Loan Fund

**Who can Apply for a BC-RLF Loan/ Grant/ Loan Guarantee?**

Public and private entities with control over or access to the site located in the City of Racine. Applicants must possess acceptable credit history, propose credible property reuse plans, provide adequate collateral, and demonstrate the financial capacity to undertake the project.

Applicants MUST have an approved Remedial Action Plan (RAP) with the Wisconsin Department of Natural Resources (WDNR), comply with the WI Voluntary Cleanup
Program (VPLE) and claim a defense under CERCLA s. 107. Parties responsible for the contamination are not eligible to apply for cleanup funding.

Priority will be given to projects that reduce environmental threats to the community, reduce sprawl, preserve greenspace, and generate job growth and economic expansion within the City.

**Eligible Uses of Funds**

Cleanup actions associated with removing, mitigating, or preventing the release or threat of a release of hazardous materials and petroleum contamination such as:

- Erecting fences, warning signs or other site control precautions;
- Installation of drainage controls; Stabilization of berms, dikes or impoundments or drainage or closing lagoons;
- Capping of contaminated soils (if required for a cleanup activity);
- Using chemicals and other materials to retard the spread of the contamination or mitigate its effects;
- Excavation, consolidation, or removal of highly contaminated soils;
- Removal of drums, barrels, tanks, etc. that may contain contaminants;
- Containment, treatment, disposal or incineration of contaminants;
- Conducting site monitoring activities (including sampling and analysis) that are necessary during the cleanup process, or that determine the effectiveness of a cleanup;
- Costs associated with public participation, worker health and safety, and interagency coordination requirements;
- Abatement of asbestos and lead-based paint, and
- Purchase of environmental insurance.

The BC-RLF funds may be used for removal activities (including demolition and/or site preparation) only if the demolition and/or site preparation is necessary to access the environmental contamination to be removed.

**What Activities CANNOT be Funded by the BC-RLF?**

The BC-RLF may not be used for pre-cleanup environmental response activities.

Funds cannot be used to expenses incurred prior to loan closing.

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**City of Burlington Community Development Block Grant Revolving Loan Fund**

This program was designed specifically to assist businesses in the City of Burlington. The program primarily finances real estate projects, equipment purchases and limited working capital needs.

The Burlington CDBG-RLF offers a below market interest rate, currently as low as 2%. Its participation cannot exceed either 50% of the total eligible project cost or $300,000.
**Eligible Project Costs**

- Land and building purchases
- Building construction
- Equipment, furniture and fixture purchases
- Limited working capital and training costs
- Demolition, renovation, and improvements of buildings
- Purchase of rolling stock

**Fees Estimated**

- $1,000 legal fee
- 1.5% processing fee
- Out-of-pocket closing costs

**Rates & Terms**

- As low as 2.44%
- Up to 10 year term
- Up to 20 year amortization
- Key man life insurance typically required.

---

**City of Burlington Tax Incremental District #3 Revolving Loan Fund**

This program was designed specifically to assist businesses in TID #3 in the City of Burlington. This district consists primarily of the downtown area and part of Highway 36. The program primarily finances real estate projects, furniture, fixtures and equipment purchases and limited working capital needs.

The Burlington CDBG-RLF offers a below market interest rate, currently as low as 50% of Prime. Participation by the TID-RLF is typically no more than 40% of the eligible project costs or $100,000, whichever is less.

**Eligible Project Costs**

- Land and building purchases
- Façade improvements
- Equipment, furniture and fixture purchases
- Limited working capital needs
- Tenant improvements

**Fees Estimated**

- $1,000 legal fee
- 1.5% processing fee
- Out-of-pocket closing costs
Rates & Terms
As low as 2.44%
Up to 10 year term
Up to 20 year amortization
Key man life insurance typically required.

Village of Union Grove Community Development Block Grant Revolving Loan Fund
This program was designed specifically to assist businesses in the Village of Union Grove and its environs. The program primarily finances real estate projects, equipment purchases and limited working capital needs.

The Village of Union Grove CDBG-RLF offers a below market interest rate, currently as low as 2%. Its participation cannot exceed either 50% of the total eligible project costs or $300,000.

Eligible Project Costs
Land and building purchases
Building construction
Equipment, furniture and fixture purchases
Limited working capital and training costs
Demolition, renovation, and improvements of buildings
Purchase of rolling stock

Fees Estimated
$1,000 legal fee
1.5% processing fee
Out-of-pocket closing costs

Rates & Terms
As low as 2.44%
Up to 10 year term
Up to 20 year amortization
Key man life insurance typically required.

Winnebago County Small Business Loan Program
Purpose
To create jobs for low-moderate income persons through low-interest loans to business in the County of Winnebago.
**Eligible Borrower**

1. Any business legally established to do business in the State of Illinois and the County of Winnebago.

2. Applicant must be able to repay the loan and is an acceptable risk as determined by the loan committee.

3. Property must conform to use under the County of Winnebago Zoning Ordinance and any other Local, State, or Federal laws.

4. Applicant must make adequate progress toward closing of loan as determined by CDBG Staff.

5. Applicant must prove that project would not proceed but for the loan.

6. All property taxes, insurance, water bills, etc., must be current.

**Eligible Products:**

1. Property acquisition, machinery/equipment acquisition, rehabilitation, expansion, and moving expenses.

2. Adequate private sector financing is not available to complete project.

3. Jobs must be created for low-moderate income persons.

4. Loans must be matched with equity or private sector financing.

5. Rehabilitation work is eligible only when done in compliance with the Davis/Bacon Act and other applicable Federal Labor Laws.

6. After completion of project, property must comply with all applicable code, permit, and license requirements.

**Ineligible Projects**

Projects where there is adequate private sector financing.

Working capital.

Inventory.

Refinancing existing debt.

Non-fixed improvements.

Improvements/purchases made prior to closing.

Projects which can be solely funded by the applicant.

Buyouts.

Housing.

Vehicles.

Incorporation expenses.

Financing fees.
The general term is 5 years at 5% per annum. However this may be adjusted based on the applicant's needs.

Rockford Local Development Corporation Microloan Program

*Eligible Uses of Funds*

- Working capital
- Real estate
- Machinery/equipment
- Leasehold improvements
- Short-term contractor materials loans

Estimated Interest Rates As of March 2012- 6-8%.
Appendix G: SOI Bank Survey Results

Bankers were surveyed in Illinois and Wisconsin in 2011 and 2013. The Illinois survey was conducted in October 2011. At that time, the Wisconsin bankers were not willing to cooperate with the survey. The Wisconsin bankers eventually agreed to participate and completed a survey similar (most of the questions were identical) to the Illinois survey in March 2013.

The majority of respondents to both surveys represented community banks. Respondents to the Wisconsin survey were somewhat more likely to be from regional banks. Most of the responses in the ‘other’ category indicated that they were large national banks.

Figure 1. How is the financial Institution chartered?

<table>
<thead>
<tr>
<th>Category</th>
<th>IL Responses</th>
<th>WI Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regional Bank</td>
<td>7</td>
<td>19</td>
</tr>
<tr>
<td>Community Bank</td>
<td>78</td>
<td>80</td>
</tr>
<tr>
<td>Savings &amp; Loan</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Other</td>
<td>11</td>
<td>14</td>
</tr>
</tbody>
</table>

IL responses: 97, WI responses: 119.

The data on how often banks in our surveys lent to small businesses is less comparable because each survey defined ‘small business’ somewhat differently. The Illinois survey defined them as having fewer than 50 employees and less than $5 million in annual revenues. For the Wisconsin survey, they were defined as those will fewer than 500 employees and less than $5 million in net profits.

Because of the Wisconsin survey’s broader definition of small business, respondents were much more likely to have a high percentage of small business loans. Small business lending makes up over half of all loans at 85 percent of Wisconsin banks, with almost two thirds stating that over 75 percent of all loans were to small businesses.

Under the more restrictive definition of small business used in the Illinois survey, about 30 percent of banks make between 51 and 75 percent of their loans to small businesses. Small business loans make up over 75 percent of all loans at another 30 percent of Illinois banks.
Figure 2. What percentage of all loan activity at your institution in the last 12 months was for ‘small business’?

![Graph showing the distribution of loan activity.]

IL responses: 94, WI responses: 121.

When working with other organizations to assist small businesses, Illinois banks are most likely to partner with small business development centers (SBDCs), chambers of commerce, local economic developers, and community colleges. They rarely or never work with the Economic Development Administration, convention & visitors bureaus, universities or state economic developers.

Figure 3. How often does your institution work with the following organizations to assist in business support and development (Illinois)?

![Bar chart showing the frequency of collaboration.]

IL responses: 93.
Wisconsin banks are generally less likely than Illinois banks to work with partners for business support. The most frequent partners that Wisconsin banks use are chambers of commerce and local economic developers. SBDCs are used, but less frequently than Illinois banks.

Figure 3. How often does your institution work with the following organizations to assist in business support and development (Wisconsin)?

WI responses: 120.
Illinois and Wisconsin bankers had substantially different views on their local economies. The likely cause of the difference is the timing of the surveys. Illinois bankers completed the survey in October 2011. Wisconsin bankers were surveyed in 2013 when the outlook for the national economy had improved substantially.

Almost two thirds of Wisconsin bankers stated that their local economy had been improving for at least a year. This compared with just 15 percent of Illinois bankers having this view in late 2011. On the negative side, Illinois bankers were much more likely to report higher levels of business closings and decreased employment.

Figure 4. Which of the following best characterizes the local economic conditions in your region? (check all that apply)

IL responses: 94, WI responses: 122.
Bankers were asked about increases in small business loan volume over two time periods: past year and past five years. Wisconsin banks saw larger increases in small business loans compared with their counterparts in Illinois. Again, this difference is largely due to the timing of the surveys. It would be expected that banks would make more loans as the economy improves.

Over the previous year, almost 45 percent of Wisconsin bankers reported increases of 5 percent or more. Only about 25 percent of Illinois bankers reported increases greater than 5 percent. About 30 percent of Illinois banks experienced decreases in loan volume, compared with less than 13 percent in Wisconsin.

Figure 5. Indicate how your financial institution’s total number of approved small business loans has changed in the past 12 months. (select only one answer)

<table>
<thead>
<tr>
<th></th>
<th>WI</th>
<th>IL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increased</td>
<td>27</td>
<td>47</td>
</tr>
<tr>
<td>Unchanged</td>
<td>19</td>
<td>20</td>
</tr>
<tr>
<td>Decreased</td>
<td>10</td>
<td>21</td>
</tr>
<tr>
<td>Don't know</td>
<td>3</td>
<td>3</td>
</tr>
</tbody>
</table>

IL responses: 71, WI responses: 79.
The results were similar when looking back five years, although the differences were not as severe. About 42 percent of Wisconsin banks experienced loan growth of greater than five percent, compared with 34 percent of Illinois banks. Significantly more Illinois banks experienced a greater than 10 percent decline (24 percent vs. 10 percent).

Figure 6. Indicate how your financial institution's total number of approved small business loans has changed in the past 5 years.

IL responses: 71, WI responses: 79.
Illinois bankers were asked the reason for changes in small business lending (this question was not included on the Wisconsin survey). The two most common answers indicated that declines were due to a lack of demand for loans. Tighter federal regulations was the third most cited reason.

Figure 7. What is the main reason for the change in lending activities for start-up businesses in the past 12 months? (check only one)

IL responses: 69.
The top two reasons for loan requests in both states were debt consolidation and working capital. Illinois had more demand for working capital loans while Wisconsin’s top driver was debt consolidation. Wisconsin banks were twice as likely to receive requests for business expansion related loans, in part because they were surveyed at a time when the national economy has improved relative to when Illinois banks were surveyed.

Figure 8. What are the main reasons for the small business loan requests received in the past 12 months? (check all that apply)

<table>
<thead>
<tr>
<th>Reason</th>
<th>IL</th>
<th>WI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Funds to expand business into new endeavors and/or different location</td>
<td>6</td>
<td>14</td>
</tr>
<tr>
<td>Debt consolidation or restructuring</td>
<td>15</td>
<td>37</td>
</tr>
<tr>
<td>Startup</td>
<td>14</td>
<td>16</td>
</tr>
<tr>
<td>Expansion of current operations and location</td>
<td>16</td>
<td>41</td>
</tr>
<tr>
<td>Working capital for operating expenses</td>
<td>46</td>
<td>59</td>
</tr>
</tbody>
</table>

IL responses: 71, WI responses: 77.
Bankers were asked what percentage of loan applications were from new businesses, expansions of existing businesses, or debt restructuring. In Illinois, existing business expansions and debt restructuring generated the majority of applications. Very few banks received more than a quarter of their applications from new business startups. The Wisconsin results were very similar to those from Illinois for this question.

Figure 9. Illinois: Approximately what percentage of total number of small business loan applications approved by your institution in the last 12 months were for each of the following: (should total 100%)

![Bar chart for Illinois responses]

IL responses: 66.

Figure 10. Wisconsin: Approximately what percentage of total number of small business loan applications approved by your institution in the last 12 months were for each of the following: (should total 100%)

![Bar chart for Wisconsin responses]

WI responses: 73.
Most banks require between 20 and 40 percent equity participation for new business borrowers. This is true in both states. For existing businesses, many banks relax the equity requirements somewhat.

Figure 11. Illinois: On average what percentage of personal equity injection does your institution require for a business loan for new and existing businesses?

![Illinois: Percentage of Equity Injection](image)

IL responses: 70 for new businesses, 62 for existing businesses.

Figure 12. Wisconsin: On average what percentage of personal equity injection does your institution require for a business loan for new and existing businesses?

![Wisconsin: Percentage of Equity Injection](image)

WI responses: 77 for new businesses, 76 for existing businesses.
Commercial loans make about 44 percent of approved loans at Wisconsin banks. In Illinois, about 31 percent of loans are for commercial businesses. Home loans make up about one third of approved loans on average in both Illinois and Wisconsin. Illinois banks made somewhat higher percentages of loans for autos and retail businesses when compared with Wisconsin.

Figure 13. What percentage does each of the following loan categories represent in your institution’s total number of approved loans in the last 12 months?

<table>
<thead>
<tr>
<th></th>
<th>Auto</th>
<th>Home</th>
<th>Agriculture</th>
<th>Retail</th>
<th>Commercial</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Illinois</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mean</td>
<td>10.3</td>
<td>32.7</td>
<td>18.0</td>
<td>8.1</td>
<td>30.9</td>
</tr>
<tr>
<td>Minimum</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Maximum</td>
<td>50</td>
<td>80</td>
<td>80</td>
<td>60</td>
<td>90</td>
</tr>
<tr>
<td>Responses</td>
<td>63</td>
<td>63</td>
<td>63</td>
<td>63</td>
<td>63</td>
</tr>
<tr>
<td><strong>Wisconsin</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mean</td>
<td>3.9</td>
<td>33.2</td>
<td>10.6</td>
<td>8.2</td>
<td>44.2</td>
</tr>
<tr>
<td>Minimum</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Maximum</td>
<td>20</td>
<td>96</td>
<td>100</td>
<td>30</td>
<td>353</td>
</tr>
<tr>
<td>Responses</td>
<td>68</td>
<td>68</td>
<td>68</td>
<td>68</td>
<td>68</td>
</tr>
</tbody>
</table>

Banks in both Illinois and Wisconsin use a diverse set of loan products for small business lending. For all types of loans, bankers in both states most frequently responded that they use the products ‘often’. Adjustable rate loans were the most likely loan type to be used ‘rarely’ or ‘never’ by bankers.

Figure 14. How often are the following used for small business loans? (Illinois)

IL responses: 69.
Figure 15. How often are the following used for small business loans? (Wisconsin)

WI responses: 75.

Insufficient cash flow is the most likely reason cited by bankers for declining small business loan applications. Cash flow was listed as ‘always’ or ‘often’ being a factor by 86 percent of respondents in both states. Inadequate personal collateral and poor credit scores were the next most common factors. The least common reasons were loans that were too large and insufficient supplier networks.

Figure 16. How often is each of the following circumstances a factor in declining small business loan applications over the last 12 months? (Illinois)

IL responses: 70.
Wisconsin bankers were asked about documentation required as part of loan applications. For entrepreneurs at the pre-venture stage, bankers are most likely to require pro-forma financials. Balance sheets, asset summaries, and multi-page business narratives are also required by over 50 percent of bankers.

For newer businesses in operation less than two years, almost all (over 85 percent) of bankers require pro-forma financials, balance sheets, and asset summaries. Balance sheets and asset summaries continue to be important to bankers as the business matures. However, longer business summaries or narratives become less critical as the business matures. Bankers are more likely to look for single page summaries from mature businesses. Generally, banks require more information from new businesses due to uncertainty. This question was not included on the Illinois survey.

Figure 18. What types of documentation do you require from a small business loan applicant? Please check all that apply.

<table>
<thead>
<tr>
<th>Documentation Type</th>
<th>PRE-VENTURE CLIENTS</th>
<th>START-UP ENTREPRENEURS (in business 2 years or less)</th>
<th>EXISTING ENTREPRENEURS (in business more than 2 years)</th>
</tr>
</thead>
<tbody>
<tr>
<td>One-page Business Overview</td>
<td>18.6%</td>
<td>32.9%</td>
<td>45.7%</td>
</tr>
<tr>
<td>Five-page Business Summary</td>
<td>25.7%</td>
<td>42.9%</td>
<td>15.7%</td>
</tr>
<tr>
<td>Multi-Page Complete Narrative</td>
<td>51.4%</td>
<td>47.1%</td>
<td>15.7%</td>
</tr>
<tr>
<td>Pro-Forma Financials</td>
<td>64.3%</td>
<td>88.6%</td>
<td>64.3%</td>
</tr>
<tr>
<td>Balance Sheet</td>
<td>57.1%</td>
<td>91.4%</td>
<td>94.3%</td>
</tr>
<tr>
<td>Asset Summary</td>
<td>54.3%</td>
<td>85.7%</td>
<td>84.3%</td>
</tr>
</tbody>
</table>

Responses: 70
Referral to small business development centers (SBDCs) is the most common assistance provided by bankers to unsuccessful loan applicants. Over half of all bankers responding stated they provided SBDC referrals. Service Corps of Retired Executives (SCORE) was the next most common referral. Wisconsin bankers appear somewhat more likely to provide referrals. The third most common response for Illinois bankers after SBDC and SCORE referrals was ‘no assistance typically offered’.

Figure 19. What assistance does your institution routinely provide to small business loan applicants denied for a loan from your institution? (check all that apply)

IL responses: 70, WI responses: 71.
Not surprisingly because of the timing of the surveys, Wisconsin bankers were more optimistic about future small business lending growth. About 70 percent of Wisconsin bankers expected lending to increase by 5 percent or more, with over one quarter expecting a greater than 10 percent increase. Only one banker responding from Wisconsin expected a decline in small business lending. In late 2011, Illinois bankers were somewhat optimistic. Sixty percent expected at least some lending growth. Fewer than 10 percent of Illinois respondents expected a decline in lending.

Figure 20. During the next 12 months, how do you anticipate that your financial institution's level of small business lending will change? (check only one)

IL responses: 70, WI responses: 73.

The US Small Business Administration (SBA) is the organization that banks work with most often when closing small business loans. The SBA has loan guarantee and other loan programs that are designed to partner with private sector banks. About 32 percent of Illinois bankers and over 40 percent of Wisconsin banker indicated that they worked with SBA ‘often’ or ‘always’. The US Department of Agriculture (USDA) was the next most common agency for bankers to work with. Like SBA, USDA has loan programs that work in partnership with banks.

Illinois bankers only rarely work with state agencies or local revolving loan funds. This is also true of most Wisconsin agencies. However, bankers do commonly work with Wisconsin Business Development (WBD). About 80 percent of Wisconsin respondents indicated that they worked with WBD ‘sometimes’, ‘often’, or ‘always’. 
Figure 21. Indicate how often your institution has worked with each of the following agencies during the past two years in order to close small business loans. (Illinois)

Figure 22. Indicate how often your institution has worked with each of the following agencies during the past two years in order to close small business loans. (Wisconsin)

IL responses: 65.

WI responses: 69.
An open-ended question focused on collaboration with partners in the region. The question yielded diverse responses. Some said that they already were working with partners. One respondent in Wisconsin reported partnering with county economic development corporations and chambers of commerce. Others simply said that they do not. Those that suggested new activities focused on education, either suggesting that bankers learn more about available programs or better educating small business owners. Of the seven respondents in the Wisconsin survey that answered the open-ended question on collaboration, four of them stressed the importance of information sharing. Two out of twelve respondents in the Illinois survey also expressed a need for information about government programs that help banks lend to businesses. These responses are consistent with the survey’s findings regarding awareness of programs provide by state governments, SBA, and USDA.

Illinois bankers were asked about their familiarity with Advantage Illinois, the Department of Commerce and Economic Opportunity’s program to increase access to capital for small businesses. This program had been announced in the months leading up to the survey. Less than 40 percent of Illinois bankers indicated familiarity with Advantage Illinois.

Figure 23. Are you familiar with the recently announced Advantage Illinois program with regards to how it relates to institutional lenders?

![Chart showing familiarity with Advantage Illinois]

Given the low level of awareness about Advantage Illinois, it is not surprising that few bankers indicated that they would be likely to use the programs within it. About one third of bankers responded ‘don’t know/not sure’ and another third responded ‘not likely’. The total of these two responses roughly equals the number of responses indicating unfamiliarity in the above question.
Figure 24. Please indicate how likely your institution would be to use the following Advantage Illinois programs to assist small businesses.

IL responses: 65.

A series of questions were asked about regulatory changes. The first simply asked if the bank had experienced regulatory changes. About 70 percent of bankers in both states indicated that they had experienced regulatory changes in the past year.

Figure 25. Has your institution experienced regulatory changes to small business lending in the past 12 months?

IL responses: 53, WI responses: 68.
Bankers in both states felt that the changes had resulted in tighter regulations. Other one third of Illinois bankers reported ‘much tighter’ practices with another 40 percent reporting ‘somewhat tighter’. In Wisconsin, just over 20 percent responded ‘much tighter’ while about 40 percent responded ‘somewhat tighter’. Only one banker from each state felt that regulatory practices were looser.

Figure 26. What changes has your institution experienced regarding regulatory practices in the past 12 months with regards to small business loans?

IL responses: 55, WI responses: 69.
The tighter regulatory practices resulted in fewer loans in both states. Over half of the bankers responding said that the regulatory practices led to a decrease in loans. Only two Wisconsin bankers felt that the changes led to an increase in small business loans.

Figure 27. What has been the impact of regulatory changes to small business lending in the past 12 months?


In an open-ended question, survey respondents were allowed to elaborate their thoughts on regulation in relation to their small business lending. Bankers in Illinois and Wisconsin were both asked to recommend changes in government policies at any level of government that would make banks more likely to lend to new or expanding businesses. In both Wisconsin and Illinois, the most frequently mentioned government agency was the SBA. Common complaints bankers had of the SBA were that its loan guarantees were too small to justify the cost of paying a fee and taking time to apply for the guarantee. One survey respondent in Wisconsin was willing to accept smaller loan guarantees from the SBA if a simpler application process were offered. Several survey respondents in Wisconsin also believed that they could increase their small business lending if the SBA reinstated its 504 loan refinancing program, which ended in September 2012.

The second most-frequently mentioned government agency was the FDIC. One survey respondent in Illinois and two respondents in Wisconsin perceived the FDIC as having an adversarial attitude toward banks. However, survey respondents had no specific recommendations for how the FDIC could be more amenable to bankers.
By far, Illinois bankers are most familiar with SBA’s 7(a) loan program, with over 83 percent responding that they are ‘very’ or ‘somewhat’ familiar with the program. The only other SBA loan programs that had over 50 percent indicating at least a ‘somewhat’ level of familiarity were CDC/504 loans (63 percent) and SBA Express (51 percent). None of the other programs had greater than 30 percent familiarity.

Figure 28. Please indicate your familiarity of each of the following SBA loan programs. (Illinois)
In general, Wisconsin bankers were more familiar with SBA loan programs. Over 80 percent indicated that they are ‘very’ or ‘somewhat’ familiar with three SBA loan programs: 7(a), SBA Express, and CDC/504 loans. Familiarity with the 504 program was also reflected in responses to an open-ended question on policies that respondents felt would make them more likely to increase lending to small businesses. Several respondents in the Wisconsin survey expressed interest in using the 504 program for refinancing, which was permitted only between 2011 and 2012. Over one quarter of bankers responding indicated they were at least somewhat familiar with every SBA loan program except international trade loans.

Figure 29. Please indicate your familiarity of each of the following SBA loan programs. (Wisconsin)

WI responses: 69.
When asked how many SBA loans had been approved by their institution, the responses were similar to the familiarity question. Sixty percent of Illinois banks had approved 7(a) loans, 50 percent CDC/504 loans, 21 percent SBA Express, and 17 percent American Recovery Capital. No other SBA loan program had been used by more than 14 percent of Illinois banks.

Figure 30. How many small business loans has your institution approved using the following United States Small Business Administration programs in the past 12 months? (Illinois)

IL responses: 64.
Just as they had been more familiar with SBA loan products, Wisconsin banks were more likely to approve SBA loans compared with Illinois banks. Three quarters of Wisconsin banks had approved 7(a) loans, 70 percent CDC/504 loans, and 53 percent SBA Express. CAP lines, Rural Lender Advantage, Community Express, and Patriot Express were all used by between 20 and 25 percent of Wisconsin banks.

Figure 31. How many small business loans has your institution approved using the following United States Small Business Administration programs in the past 12 months? (Wisconsin)

WI responses: 64.
Bankers were asked their opinions about ways SBA could better help them work with small businesses. They indicated that eliminating fees, reducing paperwork, and increasing loan guarantees would all be helpful. No single answer among these stood out as being significantly more important.

Figure 32. What actions by the SBA would most help your institution to assist small businesses obtain capital? (pick your top 3)

The survey turned from the SBA to focus on U.S. Department of Agriculture (USDA) programs. In general, bankers are less familiar with USDA programs as compared to SBA programs. USDA’s Commercial and Industrial Loan program was the only one that Illinois bankers were at least somewhat familiar with. Three others (BI Guarantee, Rural Economic Development, and Guaranteed Company) registered over 10 percent familiarity. The remaining programs were all under 5 percent.

Figure 33. How familiar are you with each of the following USDA programs? (Illinois)

IL responses: 65.
In Wisconsin, over one third were at least somewhat familiar with the Commercial and Industrial program, one quarter had familiarity with the BI Guarantee program, and the Rural ED program had a 21 percent familiarity. Except for the Guaranteed Company Loan program (11 percent) all other programs were familiar to 6 percent or fewer Wisconsin bankers.

Figure 34. How familiar are you with each of the following USDA programs? (Wisconsin)

WI responses: 68.
As would be expected from the low familiarity numbers, very few Illinois bankers are using USDA loan programs. About 11 percent of banks responding made 1-10 Commercial and Industrial Loans. Between 5 and 8 percent reported making loans using the BI Guaranteed, Rural Economic Development, and Guaranteed Company programs. The remaining programs were being used by one or none of the banks responding.

Figure 35. How many small business loans has your institution approved using the following USDA programs in the past 12 months? (Illinois)

IL responses: 63.
Almost one quarter of Wisconsin banks reported using the Commercial and Industrial Loan program. The BI Guarantee program was used by 12 percent and the Rural ED program by 8 percent. One or two bank reported using the remaining USDA programs. Given the low awareness of most USDA programs in both states, it is not surprising that relatively few banks in the survey reported working with the USDA or approving USDA loans.

Figure 36. How many small business loans has your institution approved using the following USDA programs in the past 12 months? (Wisconsin)

WI responses: 64.
Bankers in both states would like to see USDA increase outreach and public education. This may be a reflection of the low familiarity numbers seen above. As with the SBA programs, they would also like to see USDA reduce paperwork and loan fee requirements and relax underwriting standards. In open-ended responses, two respondents in Wisconsin believed that the USDA’s BI loan guarantee program is under-funded and one respondent expressed interest in eliminating borrower time limits for the USDA’s Farm Service Agency loan programs.

Figure 36. How can the USDA improve small business access to capital through your institution? (check all that apply)

IL responses: 58, WI responses: 53.