Date: September 27, 2013

To: The Honorable Chairman and Members
   Pima County Board of Supervisors

From: C. H. Huckelberry
      County Administrator

Re: Resolution Requested by the Pima County Small Business Commission Regarding
    Creation of a Pima County Prosperity Fund Corporation

Attached you will find a Resolution, prepared by the Pima County Small Business
Commission (SBC), which is on the October 1, 2013 Board of Supervisor’s agenda for your
consideration; as well as May 29 and May 13, 2013 Memoranda from Tom Ward, Vice
Chairman of the SBC which explain the purpose and development history of this Resolution
and which include a Pima County Attorney legal opinion regarding this proposal.

In reviewing this proposal I requested that the proposal and the Resolution specifically
protect the County from both financial liability for the loans and from legal liability
regarding the provisions of Article 9, Section 7 of the Arizona Constitution, which
provides: “Neither the state, nor any county, city, town, municipality, or other subdivision
of the state shall ever give or loan its credit in the aid of, or make any donation or grant,
by subsidy or otherwise, to any individual, association or corporation”.

I also requested that the proposal not duplicate the work of existing, local small business
assistance organizations and that the commission assure that there were effective and
experienced operators for the loan program.

Paragraphs seven through twelve of the Resolution deal specifically with each of those
concerns, including especially the formation of a legally separate non-profit corporation, the
solicitation of all loan funds from private financial institutions, the recruitment of private
individuals with local lending expertise to form the non-profit corporation, and the use of
the Business Development Finance Corporation and the Microbusiness Advancement
Center to administer the loan program.

Based on this information:

1. I commend the Small Business Commission for its diligence in representing the
   interest of small businesses in Pima County and its continuing efforts to contribute
   to creating and retaining jobs in Pima County in accordance with the Pima County
   Economic Development Plan.
2. I recommend that the Board of Supervisors pass and adopt Resolution Number 2013-__.

CHH/cbc

Attachments

CC: Hank Atha, Deputy County Administrator for Community & Economic Development
    Tom Moulton, Director, Economic Development & Tourism Department
    Patrick Cavanaugh, Program Coordinator, Economic Development & Tourism
    Tom Ward, Vice Chairman, Small Business Commission
RESOLUTION NO. 2013 - ________

RESOLUTION OF THE PIMA COUNTY BOARD OF SUPERVISORS APPROVING AND AUTHORIZING THE PIMA COUNTY SMALL BUSINESS COMMISSION TO ASSIST WITH THE CREATION OF THE PIMA PROSPERITY FUND CORPORATION TO FACILITATE THE PROVISION OF PRIVATE FUNDS TO LOAN TO SMALL BUSINESSES IN PIMA COUNTY IN ORDER TO CREATE AND RETAIN PRIVATE JOBS AND INCREASE COUNTY’S PROPERTY TAX BASE IN ACCORDANCE WITH PIMA COUNTY’S ECONOMIC DEVELOPMENT PLAN.

Whereas, the Pima County Board of Supervisors created the Pima County Small Business Commission (Commission) by Resolution 2003-52 on March 18, 2003 as amended by Resolution 2009-260 on October 13, 2009; and

Whereas, the Commission is responsible for facilitating communication between Pima County and small business, evaluating County policies and regulations for their impact on small business, and helping to maintain a healthy environment in which small businesses and their employees can prosper; and

Whereas, national and state economic development organizations regularly report that small business is responsible for the creation of between 70% and 80% of all new jobs created each year in the United States and in Arizona; and

Whereas, the Commission has identified the most vexing problems small businesses face in Pima County as access to capital, and the need for both capital improvement funds and short-term operating funds, such as lines of credit; and

Whereas, while the Great Recession has ended, the recovery is painfully slow, and in some sectors of the economy, even faltering; and

Whereas, the Commission has explored the possibility of creating a mechanism for a revolving loan fund to be operated as a public-private partnership by investigating similar partnerships in other states, with particular interest in loan criteria and the due diligence process; and

Whereas, the Commission met with four nonprofit agencies in Pima County that are involved in assisting small business to insure that the Commission’s revolving loan fund to be named the Pima Prosperity Fund (PPF) did not duplicate their efforts, and these four agencies encouraged the Commission to move forward; and

Whereas, the Commission is prepared to facilitate the creation of the PPF by seeking funds from local private financial institutions to finance the initial loan pool and to ask five representatives of the local financial community with lending experience, to form a nonprofit corporation, Pima Prosperity Fund Corporation (PPFC), to carry out the PPF mission and to serve as the PPF Loan Board, with the Chairman of the Commission serving as an ex-officio member of the PPFC; and
Whereas, the PPFC will work with the Business Development Finance Corporation which has agreed to handle the initial contact and screening of loan applicants, loan processing and administration; and

Whereas, the Microbusiness Advancement Center has agreed to assist loan applicants in the preparation of loan applications; and

Whereas, this structure will allow the Commission to achieve its goals of creating a private funding source to assist small business in retaining and creating jobs and additional tax base in Pima County while ensuring that Pima County has no control, responsibility or obligation regarding recipients of PPF loans, and that Pima County has no liability should a loan default.

Now, therefore be it resolved by the Board of Supervisors of Pima County that the Pima County Small Business Commission is authorized and directed to assist with the creation of the private, nonprofit Pima Prosperity Fund Corporation and the private Pima Prosperity Fund, subject to the requirements of this Resolution, for the purpose of aiding the small businesses of Pima County and creating and retaining jobs and additional tax base in accordance with Pima County's Economic Development Plan.

Passed and Adopted on: October ____, 2013

Pima County, a body politic and corporate of the State of Arizona:

______________________________
Chairman, Board of Supervisors

Approved as to Form:

______________________________
Deputy County Attorney

Attest:

______________________________
Clerk, Board of Supervisors
Memorandum

To: Tom Moulton, Director, Economic Development and Tourism

From: Tom Ward, Vice Chairman, Pima County Small Business Commission

Date: May 29, 2013

Subject: Pima Prosperity Fund Revisions

Thank you for arranging yesterday’s meeting with Deputy County Attorney, Regina Nassen, Patrick Cavanaugh of your Department and yourself. The meeting was most helpful in clarifying the issues raised by the County Administrator, Hank Atha and my memorandum of May 13, 2013 concerning the proposed Pima County Prosperity Fund (PPF).

Based upon the meeting, I will recommend to the SBC the following modifications to the PPF proposal:

1. The Small Business Commission (SBC) will recommend five members for the Proposed PPF Loan Board, all with lending experience, and ask these five individuals to form a nonprofit corporation for the purposes of carrying out the PPF mission. The Corporation will be called the Pima Prosperity Fund Corporation (PPFC). The Chairman of the SBC will be an ex-officio member of the PPFC.

2. The SBC will provide an attorney (hopefully, pro bono) to handle the legal work necessary for incorporation.

3. The PPFC will contract with the Business Development Finance Corporation (see my May 13, 2013 memorandum) to handle the initial contact and screening of loan applicants. This person will replace the executive director position and will be the face of the PPFC.

4. The loan processing and administration will be handled by a new subsidiary of The Business Development Finance Corporation – the BDFC Advisory Services LLC. This is the same organization that handles similar activities for the IDA. Gary Molenda, President of BDFC, has agreed to this arrangement.

The above four modifications do not in any way change or diminish the SBC’s intent or The mission of the PPF which is to create a funding source to assist small business in
retaining, expanding and creating jobs and additional tax base in Pima County. The modifications do ensure that the County has no control, responsibility or obligation as to who receives a PPF loan by removing any county employee form the loan process. It also ensure that the County has no liability should a loan default.

While not part of the subject of this memorandum, it occurs to me that by divorcing the County from all activities including, obviously, any fees, it would be appropriate to provide the PPFC—as an outside nonprofit entity—with a grant to handle start-up costs. I would be glad to discuss this at your convenience.

Again, my thanks to you and to MS. Nassen and Mr. Cavanaugh for assisting the SBC in this important endeavor. Please feel free to contact me if you have any questions.

C: Regina Nassen, Deputy County Attorney  
Patrick Cavanaugh, Program Coordinator, Economic Development and Tourism
Memorandum

To: Hank Atha, Deputy County Administrator for Community and Economic Development

From: Tom Ward, Vice Chairman, Pima County Small Business Commission

Date: May 13, 2013

Subject: Pima Prosperity Fund

The purpose of this memorandum is to request that the Board of Supervisors approve the creation of the Pima Prosperity Fund – a revolving loan fund designed to assist small business in retaining, expanding and creating jobs and additional tax base in Pima County.

Background

On April 19, 2012, the Small Business Commission approved the concept of a Pima County Small Business revolving loan fund. The concept was included in a memorandum entitled “Integration of a Small Business Revolving Loan Fund with the Proposed Regional County-based Business Resources OneStop Center.” (See Attachment 1.)

On July 3, 2012, the County Administrator sought a legal opinion from the Chief Civil Deputy County Attorney on the legality of such a fund, and asked five specific questions generated from the April 19, 2012 memorandum. (See Attachment 2.) These questions concerned the legality of making the loans, terms and conditions of the loans, type of collateral and sources of any public loan funds i.e. federal, state and County General Fund.

On July 12, 2012, the County Attorney’s office responded to the County Administrator’s inquiry. (See Attachment 3.) The opinion from the County Attorney’s office approved the concept of the Pima Prosperity Fund – a County revolving loan fund designed to increase small business activity by creating and retaining more jobs in Pima County. The opinion stated: “There is clearly a public purpose for the proposed loan program.”
However, the County Attorney warned that if the fund were legally challenged: "The [loan] agreements be structured in a way that exacts some promised from the borrowers regarding number of employees, pay scales, etc; something to point to as consideration for the favorable terms of the loans."

In the County Administrator's transmittal of the opinion to the Commission, he stated that the Commission, "should proceed very slowly and carefully with the development of a revolving loan fund." He also urged caution in developing, "the type of revolving loan fund" to insure "we are on solid legal footing."

On August 7, 2012, as part of the Commission's Annual Report to the Board of Supervisors, the Commission Chairman outlined the Commission's projects for fiscal year 2012-2013, including the preparation of an implementation proposal for the Pima Prosperity Fund. The Board of Supervisors accepted the Commission's Report.

This memorandum is the implementation proposed for the Pima Prosperity Fund.

Original Proposal

One of the most vexing problems small business faces is access to capital. In our discussions with small businesses of every type, this problem arises; the need is for both capital improvement funds and short-term operating funds, such as lines of credit. While the Great Recession has ended, the recovery is painfully slow, and in some sectors of the economy, even faltering.

During this last year, the Commission explored the possibility of creating a mechanism for a County revolving loan fund to be operated as a public-private partnership. The Commission investigated similar partnerships in other states, with particular interest in loan criteria and the due diligence process. The Commission also called on the assistance of the federal Small Business Administration.

While some other such revolving loan funds utilize CDBG funds to sustain their loan pools, the Commission does not believe this would be necessary in Pima County. We believe local financial institutions — and perhaps some businesses — would fund the loan pool.

The revolving loan fund, which the Commission has named the Pima Prosperity Fund (PPF), could make loans to small businesses, as defined by the County, i.e. 100 employees or less, for both capital and operating costs. Originally, the Commission envisioned a five-member Loan Review Committee composed of representatives from the private financial community. Loans below $50,000 would be approved by the
Commission; loans above $50,000 would be approved by both the Commission and Board of Supervisors.

In the days following the Board of Supervisors presentation, two supervisors expressed concern about the Board being involved in the approval of any PPF loans. Both felt it would be better if an independent organization – distanced from the Board – made the loan approvals.

This concern is addressed in the Recommendations Section below.

Other Loan Funds Serving Pima County

While not part of the its opinion approving the concept of the PPF, the County Attorney’s Office raised the concern with you that the PPF might be “duplicating” a loan service to small business already provided by other public and/or nonprofit entities in Pima County.

This proved not to be the case.

The Commission routinely reviewed the activities of the four nonprofit organizations that have provided loans in Pima County in the preparation of its original PPF concept. However, it was felt that a formal meeting with a principal of these organizations would resolve the concern about duplication. It would also give these organizations an opportunity to comment on the PPF.

Microbusiness Advancement Center

On September 20, 2012, the Commission met with Michael B. Landy, Executive Director of the Microbusiness Advancement Center. You will recall that the Commission has a history with this organization. The Commission played a significant role in the relocation of the federal government’s Small Business Administration (SBA) Small Business Development Center (SBDC) when it was in danger of leaving Pima County after the loss of its host sponsor, Pima County Community College.

In federal fiscal year 2009, the SBDC had created more than 450 private sector jobs, helped start 39 new companies and generated more than $15 million in business financing in Pima County.

After working with the Arizona SBA’s site selection committee – on which the Commission Chairman served -- an agreement was reached with the Microbusiness
Advancement Center of Tucson in December 2009 and the SBDC was relocated to that facility in January 2010.

The Commission learned that the Microbusiness Advancement Center, including SBDC, was no longer providing loans to small business. It is out of the loan business entirely. Since this organization was the prime nonprofit lender to small business in Pima County, the information obviously reinforced the need for the PPF. Mr. Landy encouraged the Commission to move forward with the PPF.

Because of scheduling difficulties, an ad hoc committee was appointed by the Chairman to meet with the other nonprofit loan organizations serving Pima County. The committee was composed of the Chairman, Vice Chairman, the Director of Economic Development and Tourism, and that Department’s Project Coordinator.

**Pima County Industrial Development Authority**

On December 3, 2012, the Commission’s ad hoc committee met with attorney Michael A. Slania from the Pima County Industrial Development Authority (IDA). You also attended this meeting. While the IDA does not make loans to small businesses (It serves as a public financing vehicle), Mr. Slania has considerable business loan experience. He suggested a loan board be created, separate from the Commission and the Board of Supervisors. This board would make all loan decisions. He suggested that an executive director be hired as the “face” of the loan board. This person would be a county employee and the entry point for loan applicants. He also suggested that we talk to the Business Development Finance Corporation, who works with the IDA in processing its loan activities.

In both the ad hoc committee meeting and in a later conservation with me, Mr. Slania encouraged the Commission to move forward with the PPF.

**Business Development Finance Corporation**

On February 26, 2013, the ad hoc committee met with Gary Molenda, President of the Business Development Finance Corporation (BDFC) which operates in Tucson and Phoenix. It manages the SBA 504 loan program which is the source of its funds. It provides loans for real estate acquisitions, construction and remodeling, equipment and machinery. No working capital, lines of credit, etc. is provided under SBA regulations.

The BDFC averages between 60 and 70 loans per year, with approximately 10% in Pima County and 90% in Maricopa County. The minimum loan is $125,000. The maximum loan is $10,000,000, under SBA 504 regulations. The maximum participation
Hank Atha, Deputy County Administrator for Community and Economic Development
Pima Prosperity Fund
May 13, 2013
Page 5

is 40% of the loan by the BDFC, 50% by a financial institution and 10% by the borrower. In other words, up to 90% financing for any project.

This program is similar, but more restrictive than the SBIC program described in Attachment 1. It provides up to 20-year loans at low rates established by the SBA.

Mr. Molenda encouraged the Commission to move forward with the PPF.

Accion

The ad hoc committee asked me to contact Accion whose headquarters is in Albuquerque, New Mexico. This nonprofit organization serves Arizona, Colorado and New Mexico. During March and April of 2013, I was able to reach Mr. Roberto Valdez-Beltran who is the regional Senior Loan Officer in the Tucson office of Accion. He is also the senior company official, here. I was also able to talk to Mr. Greg Anderson, in Albuquerque, who is the Senior Vice President of Finance for the company.

Accion provides micro-loans for small business. It prides itself on supporting minority business. It also provides training on financial and credit needs and offers workshops on entrepreneurial opportunities for minorities. Accion raises its own funds for its loan pool.

Accion’s average loan is $10,000. Its maximum term is 36 months and its interest rate is 12.5% fixed.

In 2012, Accion made 107 loans in Southeastern Arizona. Almost all were in Pima County. The average loan was for $9,300, for three years.

Accion seems very aggressive in its money-raising activities. We were asked on three occasions whether we were interested in hiring it to service PPF’s loans. Also, we were offered the opportunity to contribute to a guarantee fund to encourage other lenders to make more loans.

Its loan size, interest rate and additional services provided would not be a duplication of PPF’s proposed loan activities.

What Extra Value Does The County Receive From The PPF

In the County Attorney’s opinion stating that: “There is clearly a public purpose for the proposed loan program”, there is also stated the necessity of defining what “extra value” the borrower will provide to the County in exchange for the loan.
This goes to the rightful concern that we cannot violate the Arizona Constitution’s gift clause as most recently articulated is in *Turken V. Gordon* 223 Ariz. 342, 2010. If we provide the borrower with favorable terms (a lower interest rate for example) not available in the open market, what “adequate consideration” or “extra value” is the borrower providing the County through the PPF so that the loan is not considered as a “gift”?

The answer is readily available in the guidelines for lending used by public loan funds across the nation. It is even obliquely mentioned in the “loan philosophy” section of Attachment 1: “After one year’s experience, the PPF should determine an optimum ration of loan investment to job creation. (For example, a loan of $25,000 that created or retained 5 jobs would have an investment ratio of five to one, or $5,000 for each job.)” This was written prior to the County Attorney’s opinion. The opinion even mentions some of the possible “extra value” items that could be considered such as “number of employees, pay scales, etc.”

The “adequate consideration” or “extra value” concern is addressed in the Recommendations Section below.

**Recommendations**

The recommendations are based on the PPF concept outlined in the Commission’s April 6, 2012 Memorandum, Attachment 1, as modified by cautions expressed by the County Administrator, (Attachment 2), suggestions by the County Attorney’s office, (Attachment 3) and information gathered by the Commission’s PPF ad hoc committee.

The PPF should be implemented as follows:

**Structure**

The PPF would be composed of the following elements:

1. A PPF Executive Director, who is a qualified loan officer, would take applications, perform initial due diligence and serve as the first level of screening for any loan applicant. In essence, this person would be the “face” of the PPF. The Executive Director would be assigned to the Department of Economic Development and Tourism. I anticipate that, initially, this would be a part-time position (20 hours per week for fund-related activities). The cost for this position would be partially offset by charging a 2.5% origination fee for every loan successfully processed.
2. A PPF Loan Board would be appointed by the Small Business Commission, composed of five members of the private investment community – including both banks and credit unions. The chairman of the Small Business Commission would serve as an *ex officio* member of the Committee. This Board would review the recommendations of the Executive Director, do further due diligence as needed and approve or deny any loan application.

The Small Business Commission would not be involved in any loan decision. It would serve as the appointing agency and be an advisory group on matters of policy.

**Funding**

The loan pool would be funded by local financial institutions. It is also possible that some private firms might be interested in making dedicated investments to fund loans for small business in a specific industry, i.e. aerospace firms for small business related to aerospace activities. The minimum initial loan pool should be $2.5 million.

While most other such revolving loan funds utilize CDBG funds to sustain their loan pools, the Commission does not believe this would be necessary in Pima County.

**Small Business Eligibility Requirements**

The eligibility requirements for a small business to apply for a loan from the PPF are identical to the membership requirements of the Small Business Commission and the Board of Supervisors requirements for professional services firms seeking local preference status.

The small business must:

1. Employ no more than 100 employees.
2. Be located in Pima County (may be a branch or division of a larger business)
3. Be a for-profit business
4. The owner or manager must live in Pima County
5. A majority of employees must live in Pima County.
Loan Philosophy

With regard to philosophical loan principles, the following are important since the whole purpose of the PPF is to increase small business activity by creating and retaining more jobs in Pima County:

1. Loans should be as easy to obtain as possible, subject to sound due diligence, with minimum paper work.

2. Interest rates should be as low as possible, always below prime. The PPF is interested in creating jobs, not making money.

3. The PPF should seek lending partners wherever possible.

4. The PPF will always take the subordinate position in loan repayments.

5. While capital improvement loans i.e. land, new buildings, reconstruction or repairs, machinery, fixtures, furniture, etc. are more readily capitalized. The PPF will also consider working capital loans, lines of credit, etc.

6. Interest only for certain time periods, as well as balloon payments, should be considered where practicable.

7. While maximum loan amounts will be governed by the size of the loan pool, the minimum loan should be no less than $5,000. (This is an important point for some Commissioners.)

8. The PPF will operate under the open meeting law statues of the State of Arizona.

Adequate Consideration and/or Extra Value

In order to insure that any loan is not considered a “gift” under the Arizona Constitution. The following requirements must be enforced as conditions for obtaining a loan from the PPF:

1. A specific number of new jobs must be created over a specified length of time.

2. Wages for jobs created must meet or exceed the average for that specific job category in Pima County.

3. Retained jobs may be considered, but they must meet the same criteria as new jobs.
4. The amount of the loan must be tied to the number of jobs involved.

5. In capital improvement loans, a specific tax-generating investment must be guaranteed.

6. Failure to meet any of these loan conditions will require immediate repayment of the entire loan.

Conclusion

The Commission approved the implementation plan for the PPF at its January 17, 2013 meeting. The information obtained by the ad hoc committee during February through April has not changed this concept.

While the Commission would like to move forward quickly as possible, we believe the County Attorney should review our response to the "gift clause" contained in the Adequate Consideration and/or Extra Value portion of the Recommendation Section of this memorandum.

Also, we would like an opinion on the commission's authority to appoint the PPF Loan Board as outlined in the Structure portion of the Recommendations Section. As the memorandum states, this concept was developed to address the concerns of two Supervisors, as well as the comments by Attorney Slania of the IDA. Based upon our bylaws, the Commission believes it has such authority, particularly since the PPF Loan Board would be loaning private funds.

On a personal note, I would like to thank you for your encouragement during the gestation of the PPF. I have been a believer in revolving loan funds for small business for many years. During the last two years, your support has been very important to me.

On a similar note, I want to thank Ken Goodman. First, as my Vice Chairman and now as my Chairman, he has never waivered in his backing of the PPF.

The PPF can be a major factor in the County's Economic Development Plan. I urge you to support it.

I also urge you to be an advocate for the PPF with the County Administrator who has always supported the Small Business Commission — so that he will recommend its approval to the Board of Supervisors.

I thank you for your attention to this important matter.
Attachments: Three

c: The Chairman and members, Pima County Small Business Commission  
C.H. Huckelberry, County Administrator  
Tom Moulton, Director, Economic Development and Tourism  
Patrick Cavanaugh, Program Coordinator, Economic Development and Tourism
Memorandum

To: Ken Goodman, Chairman, Small Business Commission
   Tom Moulton, Director, Economic Development and Tourism

From: Tom Ward, Vice Chairman, Small Business Commission

Date: April 6, 2012

Subject: Integration of a Small Business Revolving Loan Fund with the Proposed Regional County-Based Business Resources OneStop Center

The purpose of this memorandum is to expand the concept of a OneStop Business Resources Center to include a revolving loan fund application center for Pima County's small businesses.

I. Background

On August 2, 2011, the Board of Supervisors accepted a recommendation from the Small Business Commission to explore the possibility of creating a mechanism for a County revolving loan fund to operate as a public-private partnership. This memorandum is the result of that recommendation.

One of the most vexing problems small business faces is access to capital. In our discussions with small businesses of every type, this problem arises; the need is for both capital improvement funds and short-term operating funds, such as lines of credit.

The Commission has investigated revolving loan fund models in Arizona, Illinois, Iowa, Ohio and Virginia, with particular interest in loan criteria and the due diligence process. We have called on the assistance of the federal Small Business Administration to investigate Small Business Investment Corporations (SBIC's).
The results of these investigations are summarized in Chart One, below.

### Chart One

<table>
<thead>
<tr>
<th>Metropolitan Area Loan Fund Jurisdiction</th>
<th>Population (thousands)</th>
<th>Revolving Loan Fund Vehicle</th>
<th>Funding Sources</th>
<th>SBIC</th>
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</thead>
<tbody>
<tr>
<td>Dayton Metro, OH City of Dayton</td>
<td>842 170</td>
<td>Citywide Development Corp. (private nonprofit)</td>
<td>1. CDBG 2. SBA 3. Private Investment 4. Loan Repayments</td>
<td>Yes</td>
</tr>
<tr>
<td>Hampton Roads Metro, VA Newport News/Hampton</td>
<td>1,700 324</td>
<td>Newport News City Council Newport News Housing Authority</td>
<td>1. CDBG 2. Loan Repayments</td>
<td>No</td>
</tr>
<tr>
<td>Quad Cities Metro, IL/IA Rock Island County, IL Scott County, IA</td>
<td>380 380</td>
<td>Bi-State Regional Planning Commission*</td>
<td>1. CDBG 2. Loan Repayments</td>
<td>No</td>
</tr>
<tr>
<td>Tucson Metro, AZ City of Tucson Unincorporated Pima County</td>
<td>1,000 520 353</td>
<td>None** Small Business Commission Board of Supervisors</td>
<td>1. SBA 2. Private Investment 3. Loan Repayments</td>
<td>Application would be considered</td>
</tr>
</tbody>
</table>

*Similar to PAG.

** Recently a group of Tucson area citizens has begun the formation of a nonprofit 501(c)3 corporation to serve as a revolving loan fund for nonprofit corporations.

The initial assumption was that the small business revolving loan fund would serve small business in unincorporated Pima County, and the chart reflects that assumption in its population entries taken from the 2010 U.S. Census. However, I believe the recommendations in this memorandum are equally valid if the jurisdiction were to cover all of Pima County.
The far right column is labeled SBIC which stands for Small Business Investment Corporation. There are more than 340 of these corporations in the nation, including two in Arizona (both in Phoenix). They are authorized and licensed by the federal Small Business Administration (SBA). In essence, a SBIC designation gives the loan fund the imprimatur to participate as a partner in various SBA loan programs, including the availability of SBA funds. It can be a major advantage in packaging loans from multiple sources for a small business.

Newport News, Virginia and the proposed Pima County loan fund both use elected public bodies in combination with publically appointed boards to administer their funds. Dayton, Ohio and the Illinois and Iowa Quad Cities use outside organizations. Dayton’s fund vehicle is a private non-profit organization with wide business and citizen participation. The Quad Cities is similar to PAG with a representation of all jurisdictions in Rock Island County, IL and Scott County, IA.

With regards to funding sources, all three loan funds use CDBG funds. For Newport News and the Quad Cities, this is the primary source of new funding. However, in Dayton, where the fund has been in operation for more than 25 years, the main source of funding is private investment (banks), SBA and loan repayments. In the interests of full disclosure, it should be noted that in past years I have worked with both the Virginia and Ohio funds.

II. Structure

For the further purposes of this memorandum, I have named the proposed Pima County small business revolving loan fund the Pima Prosperity Fund (PPF).

The PPF would be composed of the following elements:

1. A qualified Loan Officer to take applications, perform initial due diligence and serve as the first level of screening for any loan applicant.

   This person would be assigned to the Department of Economic Development and Tourism. I anticipate that, initially, this would be a part-time position (20 hours per week for fund-related activities). The cost for this position would be partially offset by charging a 2.5% origination fee for every loan successfully processed.

2. A Loan Review Committee composed of five members of the private investment community – including both banks and credit unions. The chairman of the Small Business Commission would serve as an ex officio member of the Committee. This Committee would review the recommendations of the Loan Officer, do further due diligence as needed, and make a recommendation for approval or denial of the loan application to the full Small Business Commission.
3. The Small Business Commission would act on the recommendation of the Loan Review Committee either approving or denying the loan.

Approved loans up to $50,000 would need only the Commission’s approval to be funded. Loans approved by the Commission above $50,000 would be sent to the Board of Supervisors, for final approval. The Board would not be sent loan applications that had been denied by the Commission.

III. Funding

The loan pool would be funded by local financial institutions. It is also possible that some private firms might be interested in making dedicated investments to fund loans for small business in a specific industry, i.e. aerospace firms for small business related to aerospace activities.

While most other such revolving loan funds utilize CDBG funds to sustain their loan pools, the Commission does not believe this would be necessary in Pima County. We have had very preliminary conversations with two local financial institutions who have both expressed interest in this project.

Serious consideration should be given to creating a SBIC. Such a corporation would have to be a private nonprofit company. It would be eligible for direct SBA funding for loans. Its Board could be identical to the proposed Pima Prosperity Fund Loan Review Committee. SBIC funds would be packaged with other funding sources, and would go through the same approval process as any loan described in Section II above.

IV. Small Business Eligibility Requirements

The eligibility requirements for a small business to apply for a loan from PPF are identical to the membership requirements of the Small Business Commission and the Board of Supervisors requirements for professional services firms seeking local preference status.

The small business must:

1. Employ less than 100 employees.
2. Be located in Pima County (maybe a branch or division of a larger business).
3. Be a for-profit business.
4. The owner or manager must live in Pima County.
5. A majority of the employees must live in Pima County.

6. Be in operation for at least two years.

V. Loan Philosophy

While the detailed terms and conditions of various loan packages are the rightful purview of the Loan Review Committee, certain philosophical principles must be held firmly if this public-private partnership is to fulfill its mission of retaining and creating jobs in the Pima County small business community.

Similarly, every effort must be made to make the loan process as transparent as possible, and very specific measures of accountability must be enforced to see that jobs are retained and/or created as a direct result of the loans being made.

With regard to philosophical loan principles, the following are important since the whole purpose of the PPF is to increase small business activity by creating and retaining more jobs in Pima County:

1. Loans should be as easy to obtain as possible, subject to sound due diligence, with minimum paperwork.

2. Interest rates should be as low as possible, always below prime. PPF is interested in creating jobs, not making money.

3. PPF should seek lending partners wherever possible.

4. PPF will always take the subordinate position in loan repayments.

5. While capital improvement loans i.e. land, new buildings, reconstruction or repairs, machinery, fixtures, furniture, etc. are more readily capitalized, PPF will also consider working capital loans, lines of credit, etc.

6. Interest only for certain time periods, as well as balloon payments, should be considered where practicable.

7. While maximum loan amounts will be governed by the size of the loan pool, the minimum loan amount should be no less than $5,000. (This is an important point for some Commissioners.)

8. PPF will operate under the open meeting law statutes of the State of Arizona.
9. The Small Business Commission shall make an annual report to the Board of Supervisors of PPF's activities for the previous fiscal year, including a detailed financial accounting of its loan activity.

10. After one year's experience, the PPF should determine an optimum ratio of loan investment to job creation. (For example, a loan of $25,000 that created or retained 5 jobs would have an investment ratio of five to one, or $5,000 for each job.)

Regional Reach

The Business Resources OneStop Center should have an outreach program that sends a representative, such as the PPF Loan Officer, to Ajo and Green Valley once or twice each month. This satellite operation would directly serve the small businesses in western and southern Pima County.

Recommendations

I recommend the following:

1. The concept of a small business revolving loan fund, as outlined in this memorandum, should be approved by the Small Business Commission at its April 19, 2012 meeting.

2. The fund concept, to be known as the Pima Prosperity fund, should be included as an integral part of the County Administrator's recommendation to the Board of Supervisors for a County Economic Development Program – specifically, as part of the County-based Business Resources OneStop Center.

3. The Small Business Commission should be asked by the County Administrator to flesh out the PPF concept, including the possibility of creating a SBIC, for presentation to the Board of Supervisors, in the form of an authorizing ordinance.
ATTACHMENT 2
MEMORANDUM

CONFIDENTIAL ATTORNEY/CLIENT PRIVILEGE

Date: July 3, 2012

To: Christopher Straub
Chief Civil Deputy County Attorney

From: C.H. Huckelberry
County Administrator

Re: Small Business Commission Revolving Loan Fund

Attached please find a June 20, 2012 memorandum from Tom Ward, Vice Chairman of the Small Business Commission, regarding a concept for developing a Revolving Loan Fund.

Please review the program concept and determine if the County is authorized to provide such loans, given Turken v. Gordon. The questions I have are:

1. Is the County legally able to provide the loans referenced in the memorandum?
2. If the County is legally able to provide the loans, what interest rate could the County charge, and what loan terms should be set so the loans are not construed a gift?
3. What type of collateral could the County require to secure these loans?
4. Would the County be permitted to use state or federal funds as sources for the loan bank?
5. If the County could not use state or federal funds as a source of said loans, could the County use the General Fund?

I anticipate receiving additional feedback from our Economic Development and Tourism Department to the Small Business Commission’s request.

CHH/dph

Attachment

c: Hank Atha, Deputy County Administrator for Community and Economic Development
Tom Moulton, Director, Economic Development and Tourism
Ken Goodman, Chairman, Small Business Commission
Tom Ward, Vice Chairman, Small Business Commission
Memorandum

To: C. H. Huckleberry, County Administrator

From: Tom Ward, Vice Chairman, Small Business Commission

Date: June 20, 2012

Subject: Our Conversation Concerning the Proposed Small Business Commission Revolving Loan Fund

I am pleased that you are willing to support the Small Business Commission’s (Commission) request to include its proposed Small Business Revolving Loan Fund as part of the Business Resources OneStop Center. Your June 19, 2012 memorandum on Increased County Investment in Downtown Redevelopment, including the Center, is an exciting concept.

Attached is a copy of the Commission’s proposal for Integration of a Small Business Revolving Loan Fund with the Proposed Regional County-Based Business Resources OneStop Center, which was unanimously approved on April 19, 2012. It is included in your May 25, 2011 Pima County Economic Development Action Plan.

I believe the proposal foresees any fears of the Fund’s administration by the Commission turning into an independent Rio Nuevo-type agency for the following five reasons:

1. The Commission is a creature of the Board of Supervisors.
2. The source of the loan funds is private financial institutions, not public monies.
3. The private Loan Review Committee will be monitored by the Loan Officer, an employee of the County’s Economic Development and Tourism Department.
4. All loans must be approved by the Commission.
5. Any loan more $50,000 must be approved by the Board of Supervisors, as well as, the Commission.

Recommendations two and three on Page six of the attachment specifically address the Commission’s request. Again, thank you for your support.

Attachment

c: Ken Goodman, Chairman, Small Business Commission
   Hank Atha, Deputy County Administrator for Community and Economic Development
   Tom Moulton, Director, Economic Development and Tourism
ATTACHMENT 3
CONFIDENTIAL ATTORNEY/CLIENT PRIVILEGED

Date: July 16, 2012

To: Chairman and Members
   Pima County Small Business Commission

From: C.H. Huckelberry
       County Administrator

Re: Legal Review of the Proposed Revolving Loan Fund

Attached is a July 12, 2012 Attorney/Client Privileged memorandum from Deputy County Attorney Regina Nassen of the Civil Division of the County Attorney's Office. The memorandum indicates the County should proceed very slowly and carefully with the development of a revolving loan fund.

Because of recent Arizona Supreme Court case law regarding gifts prohibited by the Arizona Constitution, I believe we must proceed very cautiously if we are to develop any type of revolving loan fund. We must first determine we are on solid legal footing in developing such a program, before the more difficult decisions are made regarding how to fund such a program.

The attached legal analysis begins the process to establish a program that is legally defensible.

CHH/dph

Attachment

c: Martin Willett, Chief Deputy County Administrator
   Christopher Straub, Chief Civil Deputy County Attorney
   Regina Nassen, Deputy County Attorney
   Hank Atha, Deputy County Administrator for Community and Economic Development
   Tom Moulton, Director, Economic Development and Tourism
To: C.H. Huckelberry, County Administrator
From: Regina L. Nassen, Deputy County Attorney
Date: July 12, 2012
Subject: Small Business Commission Revolving Loan Fund

Chuck, you asked us to review a proposed small business loan program and answer some questions regarding the County’s ability to participate in it. The program, as described in the memorandum you forwarded to us, would be funded by private financial institutions rather than with public funds. Day to day activities would be carried out by County employees, with oversight by a Commission appointed by the Board of Supervisors. Below are your questions, with our responses.

1. **Is the County legally able to provide the loans referenced in the memorandum?**

   As you know, a County can do only what it is statutorily authorized to do. There is no specific statutory authority for the County to operate such a loan program. The County does, however, have authority to “appropriate and spend public monies for and in connection with economic development activities” which are defined broadly as “any project, assistance, undertaking, program or study ... that the board of supervisors has found and determined will assist in the creation or retention of jobs or will otherwise improve or enhance the economic welfare of the inhabitants of the county.” A.R.S. § 11-254.04. Assuming there is some back-up for the proposition that this type of loan program does in fact create jobs or otherwise foster economic development in the community—and I’m assuming there is—I think a court would probably consider a small business loan program to be a legitimate economic development activity within the County’s authority, provided that it isn’t prohibited under some other statute or constitutional provision.

   It occurred to me that one might argue that this would an illegal “investment” of public funds, which, under Title 35 of the Arizona Revised Statutes, can only be invested in certain types of securities, with a maximum maturity of five years. I found no cases where such a theory was advanced, however, and it seems far-fetched to me.
2. *If the County is legally able to provide the loans, what interest rate could the County charge, and what loan terms should be set so the loans are not construed as a gift?*

See the response to Question 5, below.

3. **What type of collateral could the County require to secure these loans?**

I can't think of any legal limitation on the type of collateral used. If there is a specific reason for this concern, please let us know.

4. **Would the County be permitted to use state or federal funds as sources for the loan bank?**

I can think of no reason why the County could not use state or federal funds, provided that this use is consistent with the purpose for which the County was given the funds, with the caveat that state funds would be subject to the same constitutional limits as County funds, as discussed below. If I'm missing something, and there is a specific reason for your concern, please let us know what it is and we can follow up on that.

5. **If the County could not use state or federal funds as a source of said loans, could the County use the General Fund?**

The memorandum describing the proposed loan program states that private funds will be used for the actual loans. If that is the case, or if federal funds are used, then there is almost certainly no "gift clause" problem. If County general funds or State funds are used, however, such a loan program might be subject to challenge under art. 9, § 7 of the Arizona Constitution, which states that the County may not "give or loan its credit in the aid of, or make any donation or grant, by subsidy or otherwise, to any individual, association, or corporation."

There aren't any cases directly on point in Arizona with respect to the application of the gift clause to a loan program. The Arizona Supreme Court did, in *The Industrial Development Authority of the County of Pinal v. Nelson*, 109 Ariz. 368 (1973), hold that the statutes authorizing the creation of industrial development authorities, and the issuance by such authorities of revenue bonds to finance privately owned facilities, do not violate the gift clause. This case probably isn't of much help to us, however. When the IDA issues such revenue bonds, they are payable *solely* from the loan payments made by the private entity to which the bond proceeds (from the sale of the bonds to investors) are loaned—hence there really is no pledge of public funds or credit; the private entity is responsible for making the payments and if it defaults it will be the investors who take the hit. If County general funds are used for the loan program, as proposed here, then there are public funds at risk; hence, the IDA case is readily distinguishable.

There being no case on point, we have to apply the general gift clause test, most recently articulated in the *Turken v. Gordon* case, 223 Ariz. 342 (2010). One of the interesting things about that opinion is that the Court rejects the idea that the gift clause is violated when the transaction at issue "unduly promotes private interests" (that's helpful because if undue private benefit was the test, such a loan

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1 Note that use of bond proceeds would be problematic for arbitrage reasons, but that doesn't appear to be contemplated.
program would be more obviously problematic). Instead, the public expenditure is valid so long as it serves a public purpose and is made in exchange for adequate consideration. Consideration, of course, under Turken does not include indirect benefits such as economic development, though such benefits are a legitimate public purpose under the first prong of the test. Under Turken, “analysis of adequacy of consideration for Gift Clause purposes focuses instead on the objective fair market value of what the private party has promised to provide in return for the public entity’s payment.”

There is clearly a public purpose to the proposed loan program. Understanding how to apply the second part of the test—adequacy of consideration—in the loan context is puzzling, however. I looked for, but was unable to find, any published court opinions from other states dealing with the legality of such a loan program under a similar constitutional provision. If the interest rate and other terms of the loans are industry standard, then I think it unlikely that any constitutional challenge could be successfully brought—for such loans, the promise to repay with interest is clearly adequate consideration. But that probably begs the question; the intent is presumably to make these loans at a lower-than-market interest rate, or on somewhat easier terms, than commercially available loans. Otherwise, there would be no need for the program. So we need to identify consideration for the “extra” value that is being given to the borrower, which is represented by the gap between the program’s loan terms and what is commercially available to the borrower. Again, indirect benefits that are expected to flow from the transaction cannot be considered; we can look only at what the borrower is promising in return for the loan. I would suggest, if the County decides to move forward with this project, that the agreements be structured in a way that exacts some promises from the borrowers regarding number of employees, pay scales, etc.; something to point to as consideration for the favorable terms of the loans. That would give us something to hang our hats on in the event of a challenge.

The amount of risk to the County, if it were to go forward with such a program, and the program was successfully challenged, isn’t clear. It would depend on the amount of funding devoted to the program, and whether a court would be willing to find only a portion of the funds to have been illegally spent (perhaps the gap between the market interest rate, and the interest rate actually charged).

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2 It is interesting to note that none of the programs described in the memorandum utilize state or local public funds for the loans. They use private funds, or federal funds.