



CREDIT UNION CENTRAL OF CANADA

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Dear Ms. Ramsay:

Here is the consensus view on the Small Business Financing program, gathered from our key constituents across Canada. Responses listed directly under your questions.

Q1) Does the Canada Small Business Financing program continue to serve a useful purpose?

The credit unions that responded to our questions generally agreed that the Canada Small Business Financing Program remains useful. The program often helps start small businesses that would not have been financed in the absence of the program and small businesses contribute greatly to job creation in Canada.

Q2) Are current program parameters optimal in view of the needs of small businesses for access to financing and evolving market conditions?

The credit unions that responded to our questions outlined a number of suggestions aimed at reforming program parameters and making the program more successful. These include:

1. Consideration should be given to raising the funding amount to approximately \$500,000 with a lengthening of the amortization period to 15 years. This is especially true when realty (e.g. commercial condos) is being acquired. Many small businesses are applying through the program as they are already undercapitalized and cannot meet conventional margining requirements, and the current repayment requirements puts additional pressure on their already stressed working capital position.
2. Allow up to 10 % of the eligible expenditures to be proven by either proof of purchase or proof of payment instead of both.
3. Labor from the borrower, including that of employees, should be allowed for installation of equipment, construction or improvements. To prevent abuse, installation costs should be limited to a percentage of the value of the equipment and plans for construction or improvements would have to be prepared by a professional and would have to indicate the hours needed and the anticipated salaries to qualify.
4. The maximum amount of the personal guarantees that are permitted under the present program should be reviewed and possibly increased (e.g. from 25% of the loan amount to 50%). The program

presently permits supported guarantees from incorporation and perhaps this should extend to personal guarantees. This would be subject to the lenders review and consideration during due diligence. If the fee is to be increased to 5%, the program should allow this to be added to the \$250,000 maximum (i.e. $\$250,000 + \$12,500, 5\% \text{ fee} = \$262,500$).

5. Some credit unions recommended that the program should be expanded to include initial inventory purchases and certain goodwill items (i.e. franchise fees). Franchise fees form an integral part of the business and are essential for start up and purchases. Major franchise chains usually have good supports in place to assist the franchisees. In most instances the franchisor does impose certain performance covenants that have to be met by the franchisee. If these are not met, the franchisor reserves the right to buy back the franchise. Transactions with franchises also tend to have a lower risk factor.

6. Consideration should be given to allowing the consolidation of previously approved CSBFA loans with new advances in order to accommodate cash flow. Once again, this will also require re-examining the issue of the 10-year maximum amortization period and safeguards will have to be put in place to reduce possible abuse and undue extensions of prior advances (e.g. a special maximum amortization of 5 years for any consolidation loans).

7. Program parameters should be adjusted for start-ups during the first year of operations to include financing of technical support such as business counselor services.

8. Program parameters should be adjusted to facilitate the start up and expansion of small knowledge based firms that do not require major capital assets. In this case, the risk to the lender becomes greater as there might be minimal tangible assets which can be leveraged as security. The current CSBFA program will support equipment, buildings and leaseholds but no accommodation given to R&D and other intangible requirements for the business. For the program to be appropriate, the loan guarantee limit for these types of sectors will need to be reviewed in reducing the risk associated with financial institutions becoming involved

9. Consideration should be given to film industry similar to the above noted point in that financial institutions cannot lend against anticipated tax credits from this growing sector.

10. The program could also be expanded to include additional types of financing such as leasing and operating loans with a restriction on working capital loans say to a percentage up to 50% maximum. Also, include businesses such as community day care, golf courses etc. where they are not for profit but in reality generate profit to pay employees, debt repayment and expansion. In most cases, financing is restricted from most financial institutions.

Q3) Should the government seek to realize greater cost recovery from the program and, if so, how?

Many credit unions were skeptical about efforts to significantly expand the scope of cost recovery as it applies to the Canada Small Business Financing Program. They are concerned that increased costs borne by the borrower to further cost recovery would make the program less palatable to all. That being said, there was the suggestion that higher fees might be charged for loans in the industries where the losses are expected to be considerably higher than average. Another option would be to adjust the rules of the program to allow some forms of business restructuring or concessions to keep business going rather than simply writing loans off.

Q4) Should the program be expanded to include new types of financing for small businesses? In particular, should working capital be eligible for financing under the program?

The majority credit union position was that some defined approach to financing inventories and working capital would be refreshing. However, any extension of the program in this direction should be done carefully and conservatively to ensure that the new provisions are not abused and lead to a situation where

the program is used to increase overall debt by funding all aspects of working capital which in many cases should be accommodated through sale of inventory or collections of accounts receivables.

Q5) In view of the importance of social economy enterprises to the communities they serve, how might the program be adapted to their particular financing needs?

Credit unions noted that some social economy enterprises already have access to the program if they are operating for profit. They noted that non-profits would be more difficult to integrate into the program since they do not operate as conventional businesses, however, consideration might be given to accommodating non-profits if they pass a viability test and other special requirements (e.g. they would have to serve particular purposes such as housing, education, health, childcare; they would have to have been established for a certain number of years and have detailed annual budgets etc).

Q6) Should the interest rate on loans be deregulated (i.e. by removing the existing cap) and should the two existing two program fees (registration and administration) be integrated into a single fee.

The majority of credit unions agreed that the existing cap on interest rates should be raised to allow for increased pricing flexibility and adjustment of the rate according to loan class and industry.

There was some agreement that the current “two fee” structure was burdensome with one credit union recommending that the registration fee be eliminate and replaced with a flat \$100 annual fee. Other credit unions raised concerns about the requirement for an annual audit by an outside independent accounting firm since this is very time consuming and costly.