



South Dakota Legislative Research Council

Issue Memorandum 94-30

MICRO-ENTERPRISE LOAN PROGRAM

Introduction

The 1994 Legislature established the micro-enterprise loan program. House Bill 1393 appropriated two million dollars from the rural rehabilitation fund to the Department of Agriculture to make loans to approved development corporations. The development corporations will establish local revolving loan funds in rural areas for individuals who want to establish a small business. House Bill 1393 also established a bipartisan committee of four legislators to oversee the development of rules by the Department of Agriculture for the micro-enterprise loan program. The rules for the program are in chapter 12:07:19 of the Administrative Rules of South Dakota.

This issue memorandum explains the loan-making process and summarizes the eligibility requirements for program participants.

Loan-Making Process

A development corporation establishes a line of credit (up to \$250,000) with the Department of Agriculture. A development corporation is one of six development districts established in Executive Order 70-7, or a nonprofit multi-county development corporation approved by the Department of

Agriculture.

The applicant proposes a project to and applies for a loan (up to \$20,000) from the development corporation. The development corporation gathers the necessary financial information from the applicant and helps the applicant secure a participating lender. The participating lender may be any lender defined in section 54-3-14 of the South Dakota Codified Laws.

The development corporation sends the applicant's financial information to the Department of Agriculture. The Department of Agriculture reviews the information and approves or disapproves the loan. If approved, the Department of Agriculture disburses funds to the development corporation. The loan is serviced by either the development corporation or the participating lender.

Eligibility Requirements

Eligible applicants shall:

1. Be at least eighteen years old;
2. Propose a project that provides rural development and serves the rural agricultural community;
3. Own, operate, or begin a micro-business with gross revenues less than

\$500,000 and be located in a city with less than 25,000 population;

4. Have a principal place of business in South Dakota;

5. Be creditworthy according to the lender's standards;

6. Be unable to provide financing from the applicant's own resources; and

7. Have income equal to or less than Housing and Urban Development (HUD) median income guidelines for the county of residence. (If the income exceeds HUD guidelines, the project may be funded proportionately based on those low-income rural residents served.)

Cooperatives, corporations, partnerships, or other legal entities must meet requirements two through seven above.

Eligible projects shall:

1. Be located in South Dakota;
2. Provide direct benefit to low-income rural residents or farmers;
3. Show a potential for positive cash flow;
4. Provide an equity contribution of at least ten percent of the total project cost; and
5. Secure at least ten percent lender participation.

Eligible participating lenders shall:

1. Be subject to credit examination and supervision by an agency of the United States or of this state;
2. Be in good standing with the licensing authority; and
3. Be a local lender that provides loan services to the community where the project is located. (A lender that is not local shall maintain an office near enough to the

project location so the lender can perform loan-making and loan-servicing responsibilities.)

Other Provisions

Loan proceeds may only be used for purposes related to the project. These include purchases of machinery, equipment, inventory, and supplies; construction or renovation of buildings and facilities; purchase of land or facilities necessary to the project; and start-up operating costs. Loan proceeds may not be used to purchase, build, or renovate a personal dwelling; refinance existing debt; pay delinquent taxes; pay interest on outstanding debt; or make past due payments.

A development corporation shall pay interest annually, with the outstanding principal due in ten years or less based on the length of the loan. If a micro-business is liquidated or if a micro-business repays its loan before maturity, the development corporation shall repay its loan to the Department of Agriculture.

The interest rate on development corporation loans is based on the federal discount rate. If the federal discount rate is seven percent or less, the interest rate may not be less than the federal discount rate plus one percent. If the federal discount rate is greater than seven percent, the interest rate may exceed the federal discount rate by no more than one and one-half percent. The Secretary of Agriculture has the authority to set the interest rate.

Conclusion

The micro-enterprise loan program will provide loan funds to low-income rural residents who want to establish a small

business. The program should encourage economic development in rural areas.

This issue memorandum was written by David L. Becker, Fiscal Analyst for the Legislative Research Council. It is designed to supply background information on the subject and is not a policy statement made by the Legislative Research Council.
