2012

SMALL BUSINESS LENDING SURVEY

FLORIDA CHAMBER Foundation

CHIEF FINANCIAL OFFICER
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FLORIDA DEPARTMENT OF FINANCIAL SERVICES

ABOUT US

The **Florida Chamber Foundation** is the business-led, solutions development and research organization working in partnership with state business leaders to secure Florida's future. The Foundation's "Six Pillars" serve as a visioning platform for developing the first-ever, long-term strategic plan for the state. The Foundation's work focuses on: 1) Talent Supply and Education, 2) Innovation and Economic Development, 3) Infrastructure and Growth Leadership, 4) Business Climate and Competitiveness, 5) Civic and Governance Systems, and 6) Quality of Life and Quality Places. Founded in 1968, the Foundation is a critical voice for improving the state's pro-business climate to enable Florida to grow and prosper.

For more information, visit www.FLFoundation.org.

EXECUTIVE SUMMARY

With more than 2.2 million operating in the state of Florida, small businesses are an important part of our state's economy and local communities, making their health integral to a growing economy. Unfortunately, the small business community continues to struggle with an access to capital problem, which prevents them from obtaining the necessary means to establish, operate, or expand.

The primary lenders to small businesses are community banks and credit unions, which make nearly 40 percent of loans to small businesses nationwide, despite the fact that these small lenders comprise only ten percent of the assets in the entire financial industry. To further investigate the state's small business access to capital problem, the Florida Chamber Foundation, in collaboration with Chief Financial Officer Jeff Atwater, conducted a survey of Florida-based community banks and credit unions to better understand the strategic challenges they face and how this may be impacting small business lending throughout the Sunshine State.[1]

The survey results were overwhelming. Facing a plethora of new federal regulations and the rising cost of compliance, Florida-based community banks and credit unions are being squeezed from every direction. This is making it much more difficult to engage in a high volume of small business lending – a cornerstone of their operations and overall mission.

- Regulatory compliance is the chief strategic challenge for community banks and credit unions headquartered in Florida. Ninety-five percent of respondents said that "meeting regulatory compliance requirements" will be a significant or moderate strategic challenge over the next three years.
- Ninety-six percent of community banks and credit unions expect to spend considerably more time and money on compliance with new federal regulations over the next three years. Only 17 percent of respondents expected to spend considerably more on new state regulations.
- A majority – 64 percent – of community banks and credit unions said small business lending over the next three years will be negatively affected by the Dodd-Frank Act. Further, 72 percent said that the availability of customer services would be negatively impacted by the Dodd-Frank Act in the near future.

According to the survey results, new federal regulation is significantly and negatively impacting many of Florida's community banks and credit unions. The results suggest that new federal regulations are imposing costly burdens and unprecedented uncertainty on the primary lenders to small businesses. Further, survey respondents suggest that the Dodd-Frank Act is negatively impacting the state's small business lending community, whose institutions were certainly not the intended target of these reforms. The data suggests that these barriers may be negatively affecting small business lending and, ultimately, the state's economic recovery. A more thorough analysis of the secondary effects of recent financial regulation on community banks and credit unions may be warranted.

1 A survey form was developed by the Florida Chamber Foundation for the 2012 Small Business Lending Survey. Surveys were sent electronically via email to senior management staff of all community banks (locally owned depository institutions) and credit unions (not-for-profit financial cooperatives) headquartered in Florida with recorded total assets of $5 billion or less in 2011. The use of e-mail solicitation was the primary method for acquiring responses, which were collected through a web-based survey platform between June 15, 2012 and August 10, 2012. Among those community banks and credit unions that did complete the survey questionnaire, the median number of Full Time Equivalents (FTEs) was 37, and the median size of total assets was $210 million.

2012 SMALL BUSINESS LENDING SURVEY

Small businesses embody the spirit of innovation, entrepreneurship, and individual initiative that made this country prosperous. Today, small businesses represent the survivors of some of the most challenging economic times in decades and are the innovative leaders of continuing progress.

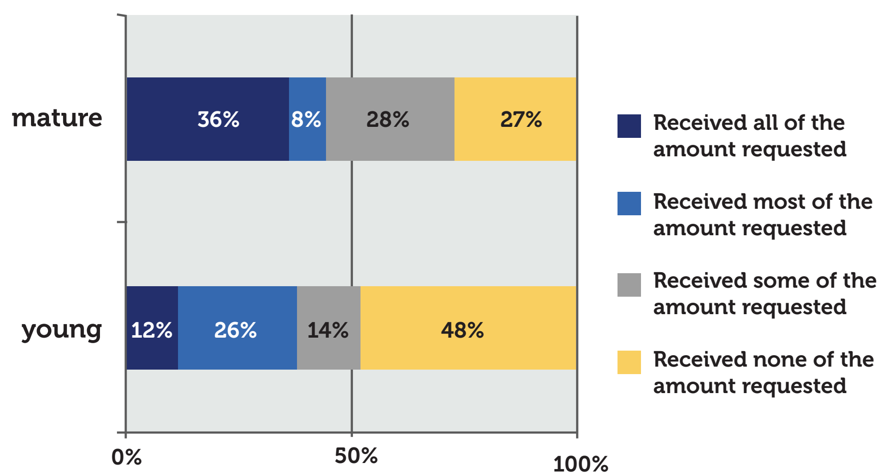
However, as Florida recovers, the small business community is disproportionately struggling to obtain the necessary means to establish, operate, or expand. Without access to the capital they need, Florida's small businesses face barriers to growth, development, and job creation, thus impeding the state's overall economic recovery. Small businesses are a key economic driver for Florida, with 2.2 million strong statewide. Collectively, they made up 98.9 percent of the state's employers and contributed $566 billion – or 75 percent of the state's Gross Domestic Product (GDP) in 2010 alone.[2] Certainly, maintaining a business environment conducive to small business development is a key ingredient for promoting economic prosperity in Florida.

The Small Business Disadvantage – Access to Capital

Small businesses across the country, and in Florida, face a significant problem: access to capital. This persistent, pervasive issue is not only hindering the growth of the small business community, but the state's full economy recovery.[3]

Capital investment allows small businesses to establish and expand operations, which is often accompanied by new job openings and opportunities. However, lending standards for loans to small businesses across the nation have remained unchanged for the fourth consecutive quarter, while lending standards for large- to mid-sized businesses have eased somewhat.[4] Throughout the Southeastern states, only two-thirds of small businesses requesting financing were able

Q1 2012 Overall Financing Satisfaction
Young and Mature Firms



Source: Federal Reserve Bank of Atlanta, July 2012

2 The Florida Scorecard; "Small Business Profile: Florida", U.S. Small Business Administration, January 2012.

3 Small businesses defined as a firm with fewer than 500 employees and annual sales of less than $50 million, as used by the Federal Reserve System.

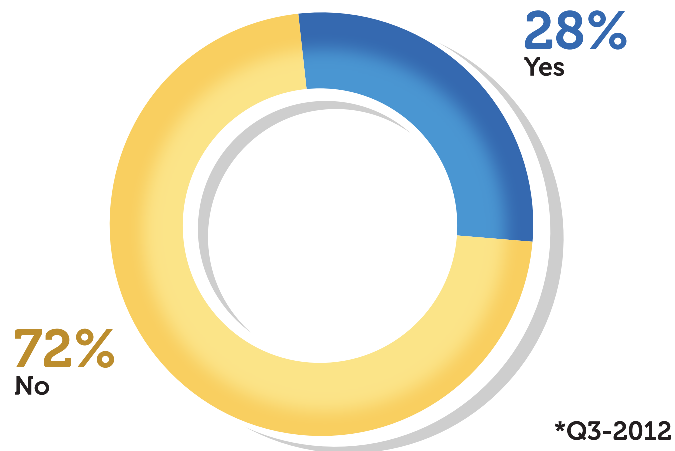
4 Loans to businesses with less than $50 million in annual sales. "July 2012 Senior Loan Officer Opinion Survey on Bank Lending Practices", Board of Governors of the Federal Reserve System, August 2012.

to obtain it. Of those who did receive financing, only a portion (12%) of those applying were able to obtain the full amount of credit requested. Further, most of the "young" firms surveyed stated that they did not seek capital because they believed they could not get it.[5]

Yet it is these same young firms, which serve as significant generators of new economic activity and jobs, that are most in need of capital in order to expand and establish their businesses. Despite submitting ten percent more credit applications in the first quarter of 2012, small businesses in the Southeast that have been open for fewer than six years received less financing than requested. In fact, half of these younger businesses (48%) did not receive any of the financing requested.[6]

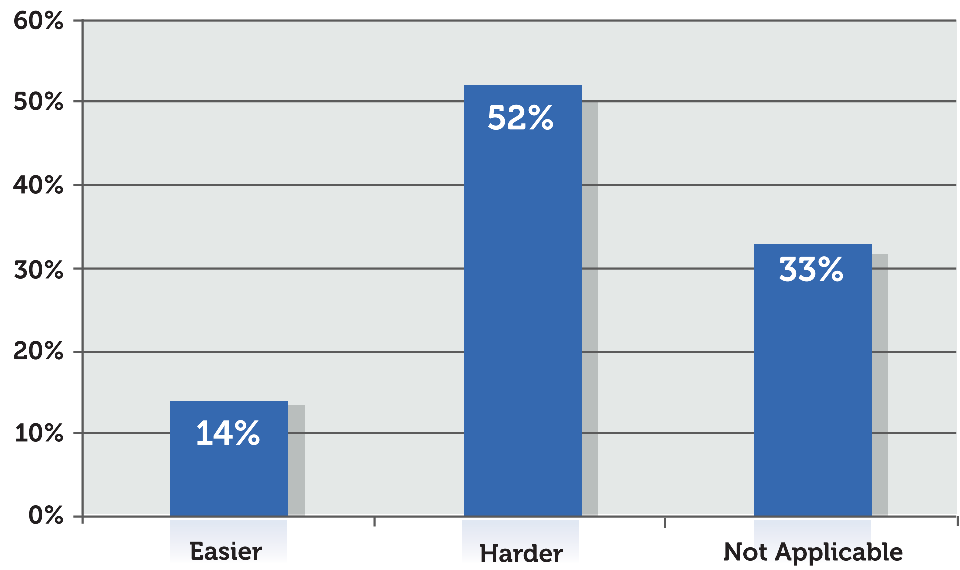
In Florida, the lending situation is similar. Many small businesses cannot obtain the financing they need to grow and add new jobs to the state's economy. Of the small businesses trying to obtain financing during the third quarter of 2012, 72 percent were unable to do so, according to the Florida Chamber of Commerce's *Small Business Index Survey*.[7] Unfortunately, a majority of these small business owners – 52 percent of respondents – said it will be harder to obtain credit over the next six months.[8]

*Of those who sought financing during the last six months, were you able to obtain it?**



Source: Florida Chamber of Commerce, Small Business Council

*Ability to Obtain Financing During the Next 6 Months**



Source: Florida Chamber of Commerce, Small Business Council

*Q3-2012

5 A "young" firm is distinguished from a "mature" firm by the age of the business, where firms less than six years old are considered to be "young", according to the Federal Reserve Bank of Atlanta. "Small Business Survey: Q1 2012", Federal Reserve Bank of Atlanta, July 2012.

6 "Small Business Survey: Q1 2012", Federal Reserve Bank of Atlanta, July 2012.

7 "2012 Quarter 3 Survey Results", Small Business Index Survey, Florida Chamber of Commerce Small Business Council. June 2012. Available at: http://www.flchamber.com/wp-content/uploads/SBC-Index-Report_June-2012.pdf.

8 Ibid.

Today, community banks and credit unions remain the key providers of valuable financing to small businesses across the nation.[9] Although lenders with less than $1 billion in assets make up only ten percent of the entire financial industry's assets, these small lenders make nearly 40 percent of loans to small businesses, making them a crucial part of the solution to the access to capital problem.[10] However, facing new regulations, the rising cost of compliance, and poor economic conditions, community banks and credit unions in Florida are being squeezed from every direction, which has made it much more difficult for community banks and credit unions to engage in a high volume of small business lending – a cornerstone of their operations and overall mission.

The 2012 Florida Small Business Lending Survey

In order to improve our state's economy, small businesses must be able to obtain the credit necessary to finance their operations and make their ideas a reality. As access to capital continues to be a small business disadvantage, the Florida Chamber Foundation, in collaboration with Florida Chief Financial Officer Jeff Atwater and the Florida Department of Financial Services, conducted the *2012 Florida Small Business Lending Survey*, which surveyed the key providers of capital to small businesses – community banks and credit unions – to better understand the challenges facing these critically important institutions who pride themselves on being able to finance their local entrepreneurs and small businesses.[11]

To capture the true population of small business lenders located in Florida, community banks and credit unions headquartered in the state with less than $5 billion in total assets were surveyed[12] between June and August 2012 to discover how they are faring under these uncertain economic and regulatory conditions, particularly with regard to their small business lending activity.

The results of the *2012 Small Business Lending Survey* were overwhelming. According to respondents, implementation and compliance with federal regulation is draining the resources of our local lenders and dampening their ability to lend to small businesses. In fact, regulatory issues were identified as the top strategic challenge facing both community banks and credit unions in Florida over the next three years. Other issues, including the growing cost of compliance, poor economic conditions, and new capital requirements, were also cited as challenges. All of these issues may prevent community banks and credit unions from providing the capital that small businesses need to make necessary investments and, therefore, grow Florida's economy.

9 "Small Business Survey: Q1 2012", Federal Reserve Bank of Atlanta, July 2012.

10 "Remarks by FDIC Acting Chairman Martin J. Gruenberg to the American Banker Regulatory Symposium; Washington, D.C.", Federal Deposit Insurance Corporation, September 19, 2011. Available at: http://www.fdic.gov/news/news/speeches/archives/2011/spsep1911.html.

11 Community banks and credit unions headquartered in Florida with less than $5 billion in total assets were sent survey, via email from June to August 2012. Throughout the survey period, there were 75 respondents from different community banks and credit unions. (See methodology section for more information.)

12 Banks and credit unions with assets less than $5 billion are considered to be relatively small in the banking world. For example, Bank of America and Wells Fargo, two of the largest banks in the nation, hold approximately $2 trillion and $1.3 trillion in total assets, respectively, and approximately 275,500 and 264,000 employees, respectively. In this survey, the median number of Full Time Equivalents (FTEs) was 37, and the median size of total assets was $210 million. Yahoo Finance, accessed 9/19/12. Available at: http://finance.yahoo.com.

Regulatory Compliance is Biggest Challenge

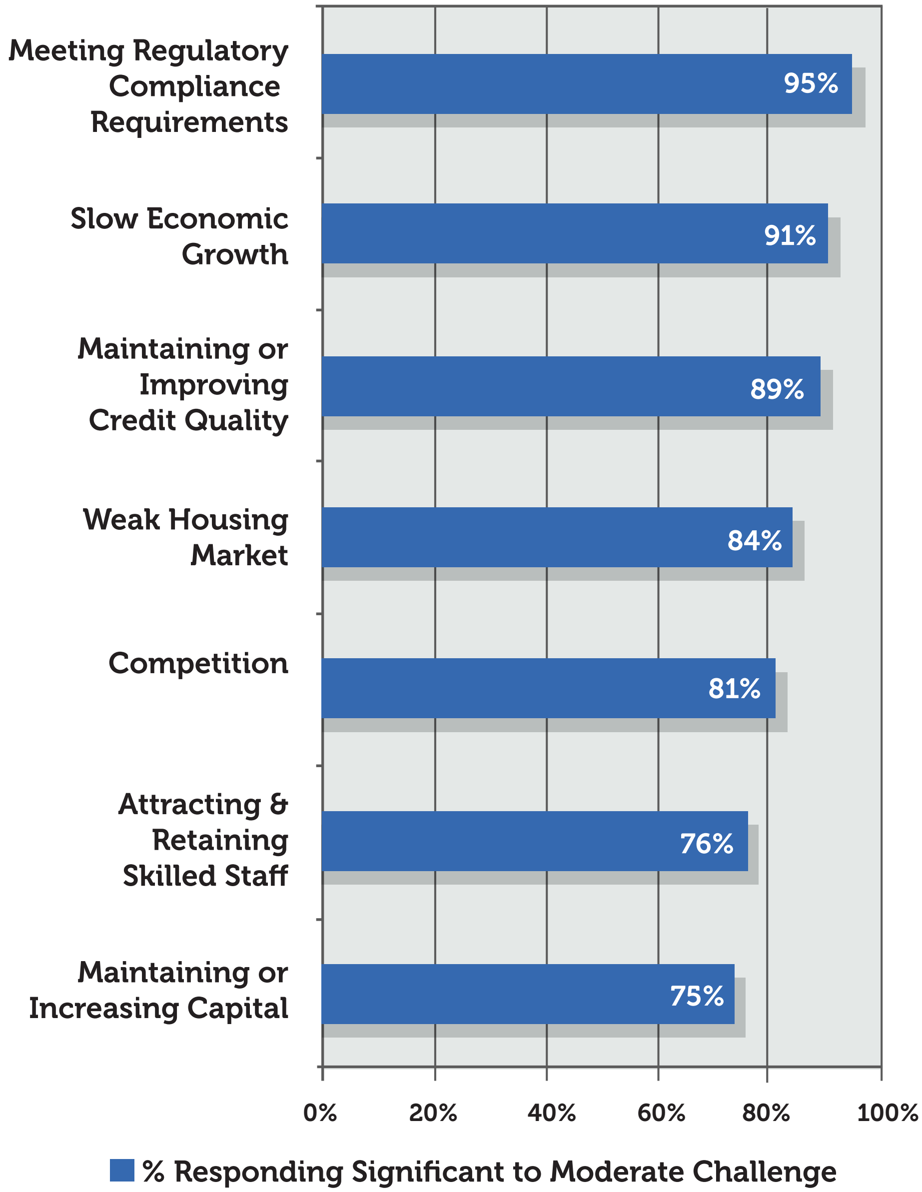
In 2012, The Economist magazine noted that one of the largest threats to America's economic recovery is the ever-growing burden of federal regulation.[13] The 2012 Small Business Lending Survey found overwhelming evidence to support the conclusion that regulation is a significant, growing burden. Survey respondents indicated that compliance with new regulatory requirements is the top strategic challenge for both community banks and credit unions in Florida.

Facing a tidal wave of new compliance issues and increased costs, these local lenders are left with fewer resources for lending to small businesses. Moreover, many of the financial regulations included in recent federal legislation have yet to be implemented, generating a climate of uncertainty for these small lending institutions.[14]

- Ninety-five percent of respondents said that "meeting regulatory compliance requirements" will be a significant or moderate strategic challenge over the next three years.

These results signal that small business lenders are concerned with government regulations, which according to survey respondents, "cost hundreds of thousands of dollars to comply with" each year.

Top Strategic Challenges Over the Next 3 Years



> *"A poor economy and excessive regulatory burdens are creating a tremendous challenge"*
>
> *- Survey Respondent*

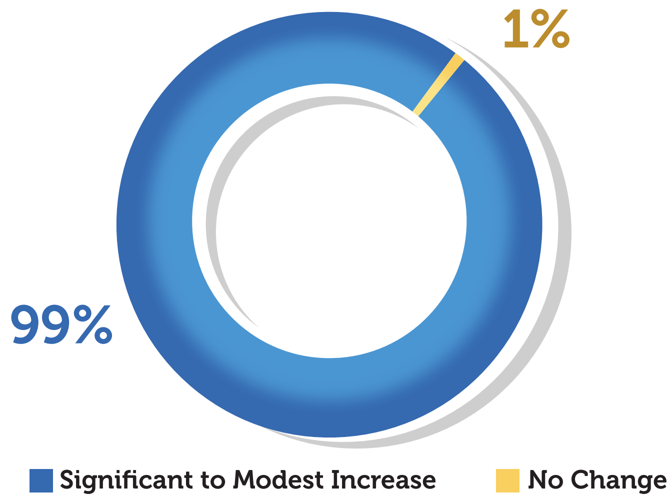
13 "Over-regulated America", The Economist Magazine, print edition. February, 18, 2012. Available at: http://www.economist.com/ode/21547789.

14 "Dodd-Frank Progress Report: Two-Year Anniversary Report", DavidPolk law firm, July 18, 2012. Available at: http://www.davispolk.com/files/Publication/15a76992-d82a-4d15-a2db-fcde9effc3d0/Presentation/PublicationAttachment/b82f9d23-0edc-49eb-af02-ff97ff34bd56/071812_Dodd.Frank.Progress.Report.pdf.

Unfortunately, regulatory compliance is a significant cost-driver for local lending institutions.

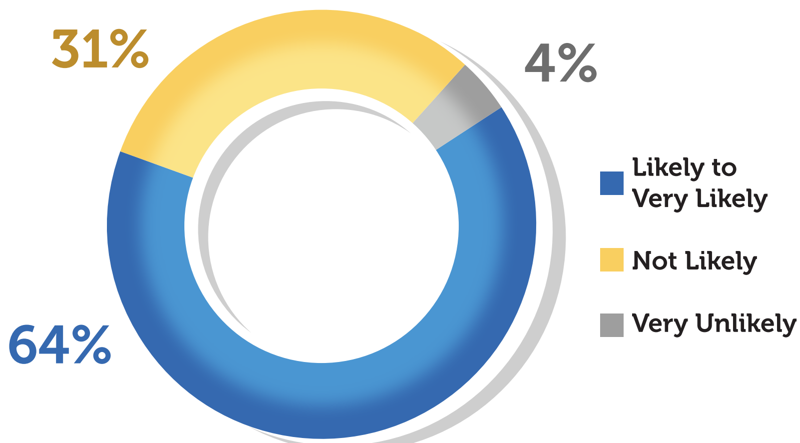
- Ninety-nine percent of respondents stated that they expect significant to modest increases in the amount of money and time spent on compliance issues over the next three years.

*How do you expect that **staff time and money spent on compliance issues** will change over the next three years?*



> *Compliance requirements divert money and time from helping customers grow and expand their businesses.*
>
> *- Survey Respondent*

% Expecting to Hire Additional Compliance Staff in Next 3 Years



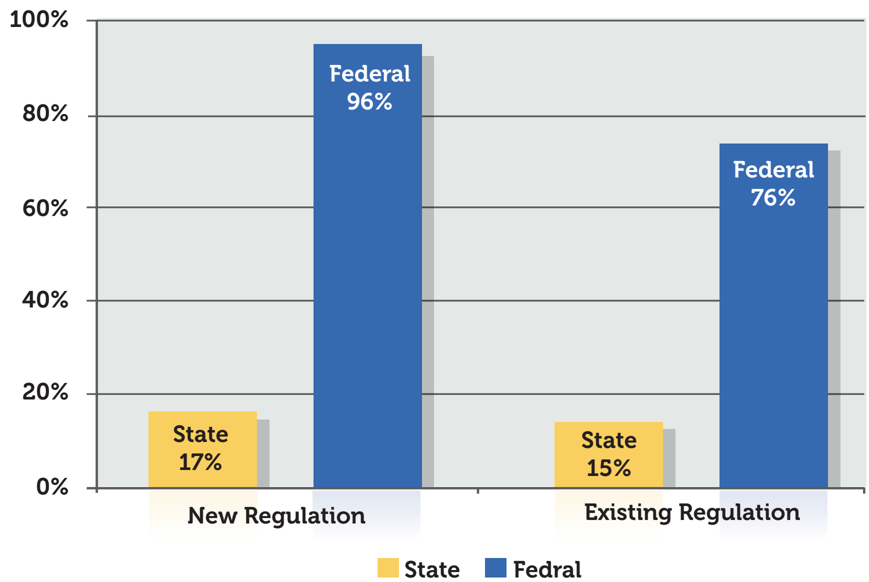
- Sixty-four percent of respondents stated that they will very likely or likely need to hire additional compliance staff over the next three years. The need for and cost of additional compliance staff may divert resources away from small business lending operations.

Federal Regulation

Since the 2007 financial crisis, volumes of new federal regulation have been placed on all areas of the financial sector from Main Street to Wall Street. According to the survey results, new financial regulations present significant challenges to local lending institutions through an expansion of regulatory requirements and oversight as well as increased monitoring of community banks and credit unions.

- Ninety-six percent of community banks and credit unions expect to spend considerably more time and money on compliance with new federal regulation over the next three years.
- Further, 76 percent of respondents also stated that compliance with existing federal regulation is a costly and time consuming issue.
- At the same time, both new and existing state regulation is much less of a concern for respondents, reflecting the relatively lower burden of state regulation on community banks and credit unions in Florida.

In which of the following areas do you expect to spend considerably more time and money over the next three years?

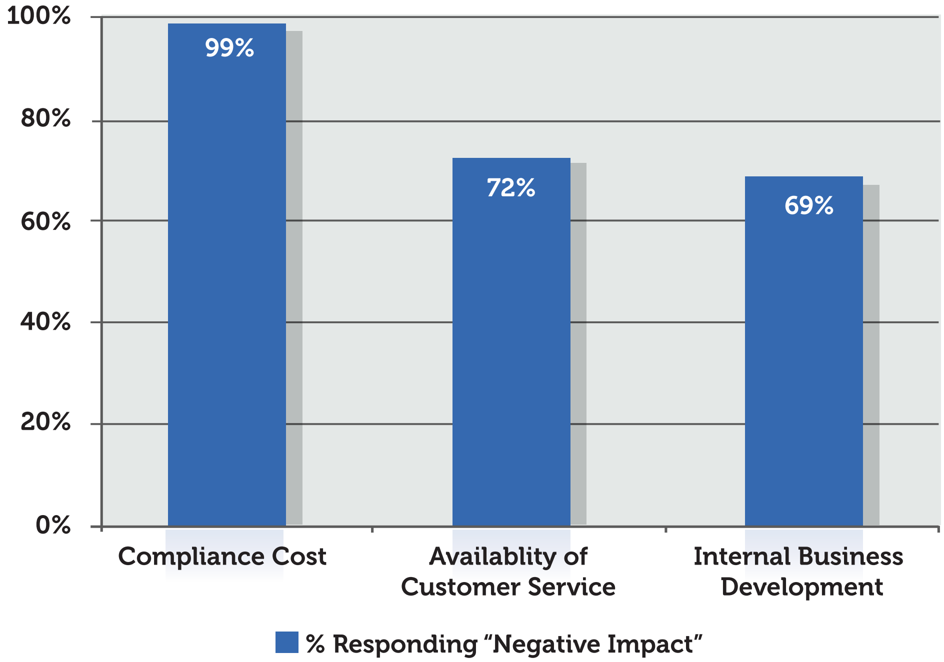


Impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010

The *Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010* ("the Dodd-Frank Act") is the most poignant example of the increasing burden associated with the current regulatory environment. The Dodd-Frank legislation was intended to target big financial institutions, large banks, and investment institutions. However, despite its focus on reigning in risky behavior by large Wall Street firms, the reform's thousands of pages of rules and regulations have created a significant degree of uncertainty or the cornerstones of our neighborhoods and communities—namely small businesses.

According to survey respondents, the Dodd-Frank Act is negatively impacting the state's small business lending community, whose institutions were certainly not the intended target of these reforms. Survey respondents cited the confusion, complexity, and inconsistencies of the Dodd-Frank Act as incurring significant collateral damage on their core operations. Under the Dodd-Frank Act, community banks and credit unions, which pride themselves on being able to finance local entrepreneurship and small business, must instead spend their resources complying with 'one-size-fits-all' regulation intended to reform larger banks and the investment institutions of Wall Street.

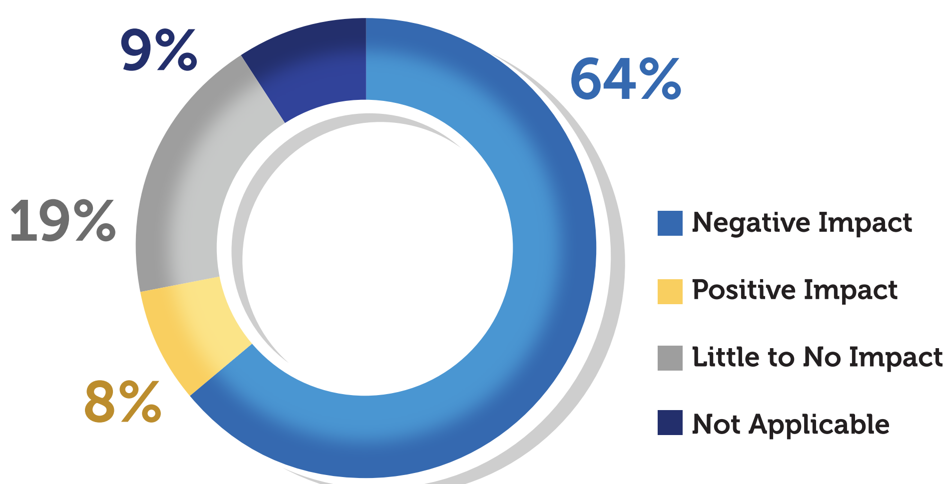
How do you expect the Dodd-Frank Act of 2010 to impact your institution over the three years?



Survey respondents overwhelmingly cited the two-year old Dodd-Frank Act as having a negative impact on their institutions across many dimensions over the next three years.

- Ninety-nine percent of respondents expect the Dodd-Frank Act to have a negative impact on their institution's compliance costs over the next three years.
- Seventy-two percent said that the availability of customer services would be negatively impacted by Dodd-Frank, while 69 percent of all respondents believe it will hinder their internal business development in the future.

Dodd-Frank's Impact on Lending to Small Businesses

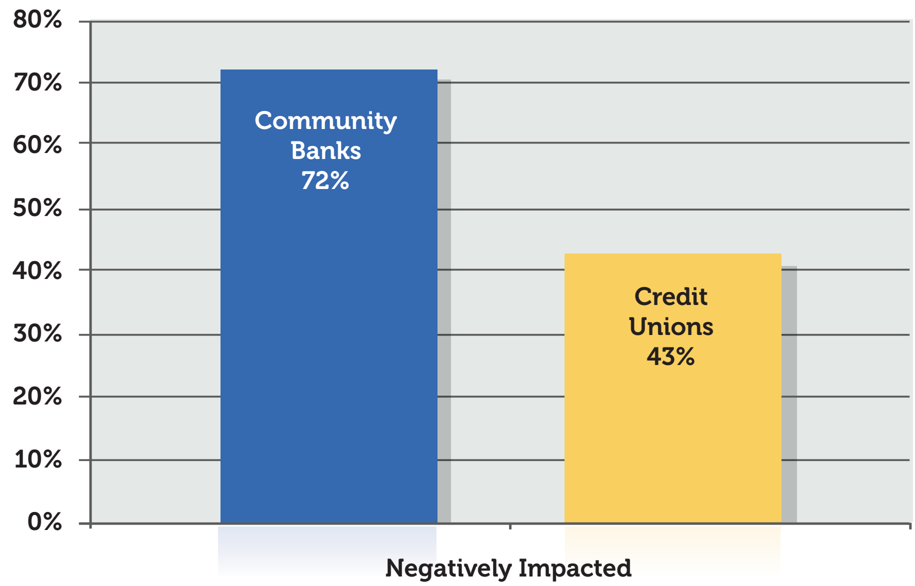


According to survey participants, the Dodd-Frank Act is forcing community banks and credit unions to divert resources to compliance issues and it is affecting their lending to small businesses here in Florida.

- A majority – 64 percent – of community banks and credit unions said their lending to small businesses over the next three years will be negatively affected by the Dodd-Frank Act.

- Examined more closely, a larger number of community banks believe their business lending will be negatively affected by the Dodd-Frank Act than did credit unions. This difference may be attributed to the fact that some credit unions do not offer business lending thus, this survey question would not be applicable. [Of the credit unions responding to the survey, 28.6% stated that business lending was "Not Applicable" to their loan operations.]

Community Banks and Credit Unions Believe Dodd-Frank will Negatively Impact their Business Lending over the Next Three Years

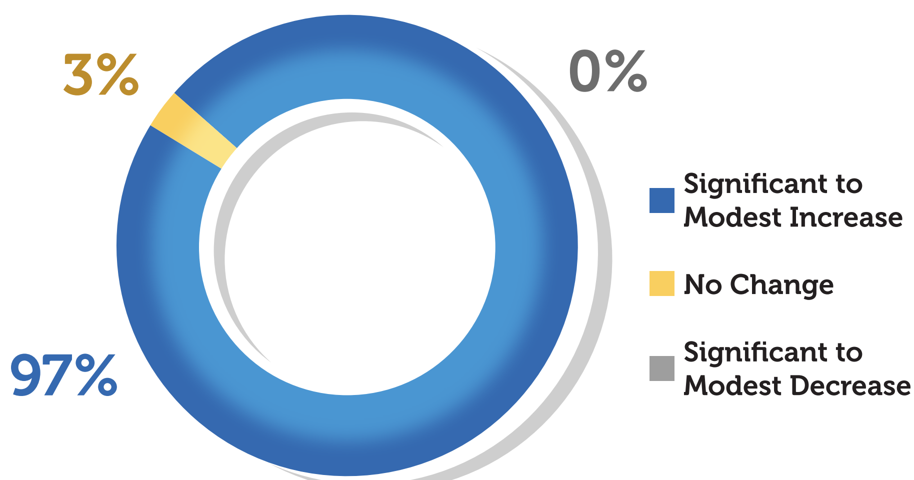


What impact does all of this federal regulation have on our local community banks and credit unions?

Senior Management More Focused on Compliance, not Lending

- Ninety-seven percent of community banks and credit unions said senior management attention to compliance issues will significantly or modestly increase over the next three years, leaving less time to find ways to attract capital and lend to small businesses in our state. A negligible amount of respondents stated that there would be no change.

How will your senior management and Board of Directors' attention to compliance and resource planning change over the next three years?



More Resources Spent on Compliance Costs, not Lending

Increased attention of management to compliance issues and resource shifting will have a negative impact on both the lending activity and operating budgets of community banks and credit unions.

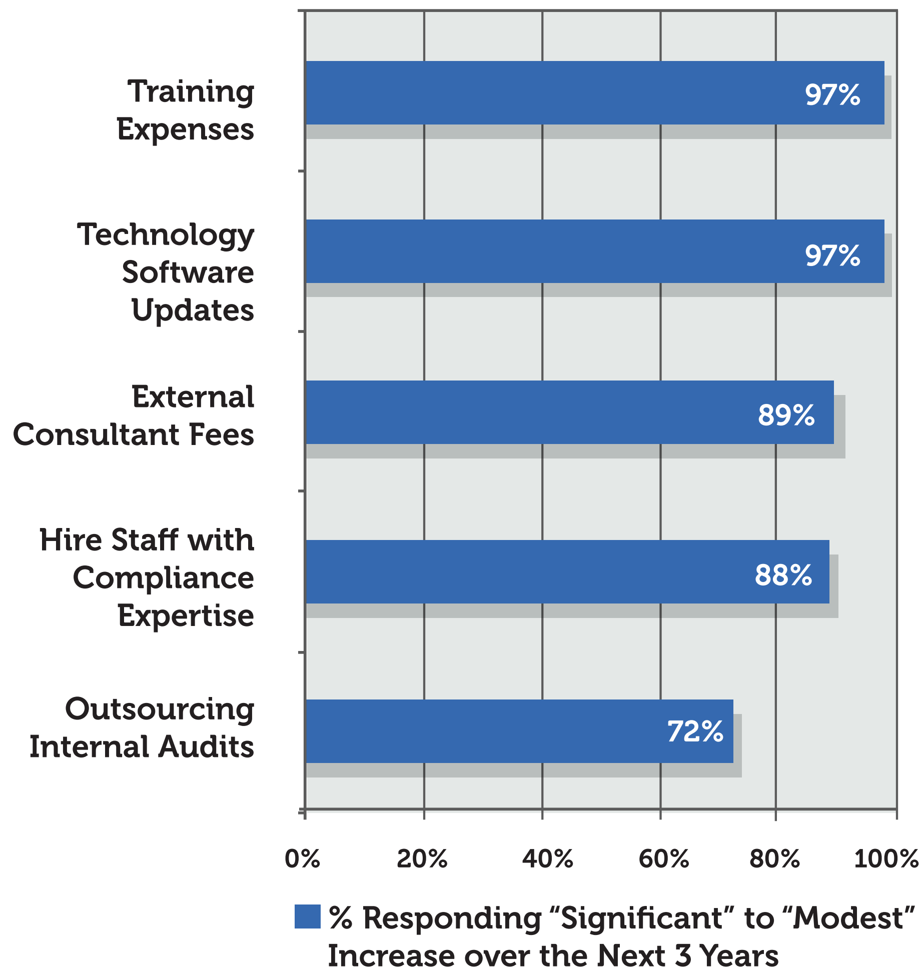
Over the next three years:

- Eighty-eighty percent of community banks and credit unions expect to significantly or modestly increase their budget for hiring staff with compliance expertise and 97 percent expect to spend more on staff training expenses;

- Ninety-seven percent expect to spend more of their budgets on technology software upgrades to deal with new reporting requirements and regulations; and,

- Eighty-nine percent believe they will spend significantly to modestly more of their budget on external consultant fees in the future while 72 percent will spend more on outsourcing their internal audits.

Impact of the following compliance management strategies on your budget over the next three years



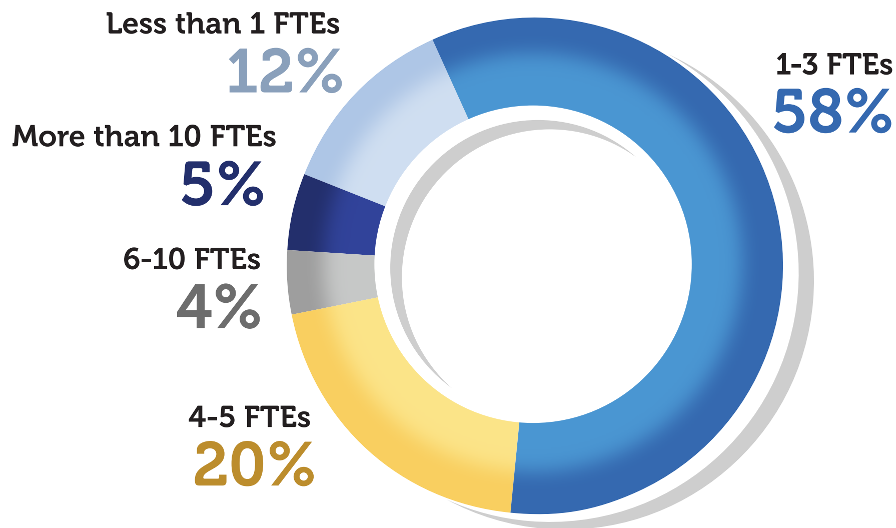
These results signal that both community banks and credit unions are diverting valuable resources from their budgets toward regulatory compliance, instead of engaging in lending that may facilitate new capital investments and job creation.

Doubling Compliance Staff, not Lending

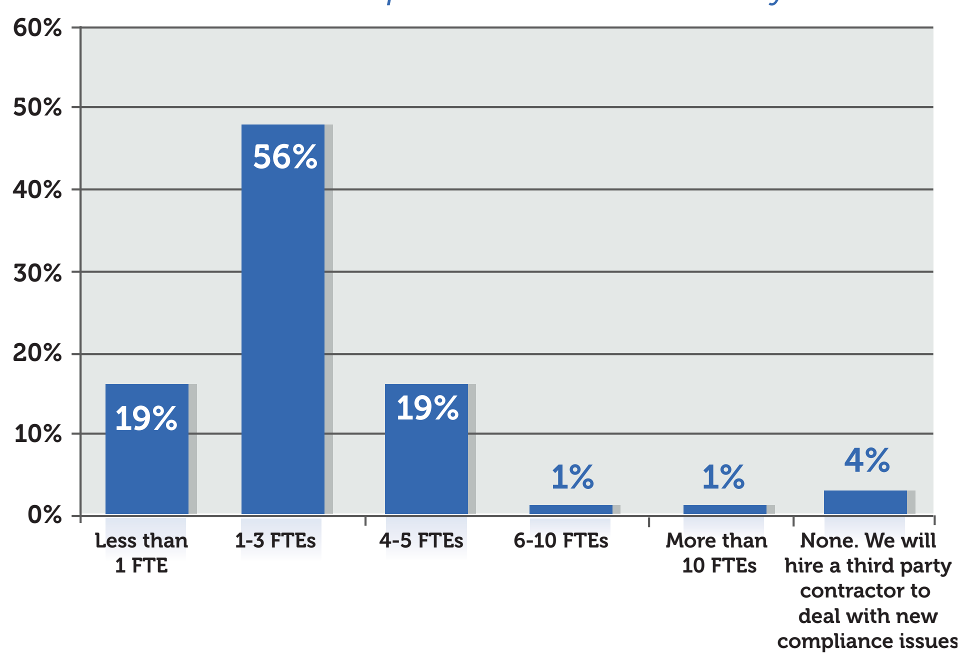
A majority of both community banks and credit unions expect they will need to double the number of full-time employees dedicated to compliance over the next three years.[14]

- A majority of responding community banks and credit unions have between one and three full-time employees currently devoted to compliance.
- Over the next three years, most of these institutions will effectively double their compliance staff as a majority of respondents anticipate that they will need to hire an additional one to three full-time employees to deal with compliance issues in the near future.
- Typically, smaller lending institutions do not have many compliance officers on staff given their size and scope of lending activities, making this increase in compliance staff significant.

How many full-time employees are currently devoted to compliance at your institution?



How many additional full-time employees do you expect to devote to compliance over the next three years?



14 Compliance officers do not typically perform the same duties as an auditor. Fifty-eight percent of respondents said they have between one and three Full Time Equivalents (FTEs) with 56% stating that they expect to devote one to three additional full-time employees for compliance issues over the next three years.

The Future?

Our best hope for getting Americans back to work and attaining a sustainable economic recovery begins and ends with the ingenuity of American entrepreneurs and small business owners. This makes it imperative that we monitor how their principal lenders, community banks and credit unions, are faring during these uncertain regulatory times.

According to the *2012 Small Business Lending Survey*, new federal regulation is significantly and negatively impacting many of Florida's community banks and credit unions. The survey results suggest that new federal regulations are imposing costly burdens and unprecedented uncertainty on the primary lenders to small businesses and these barriers to small business lending may be negatively affecting the state's economic recovery.

While many new financial regulations have positive intentions, the survey suggests that they may be restricting the flow of capital to the small businesses responsible for much of the state's job creation and economic progress. Overall, the results of the survey imply that we should consider the effects of an increasing federal regulatory burden on smaller lending institutions, those who ultimately affect the ability of small businesses to raise capital. A more thorough analysis of the secondary effects of recent financial regulation on community banks and credit unions may be warranted.

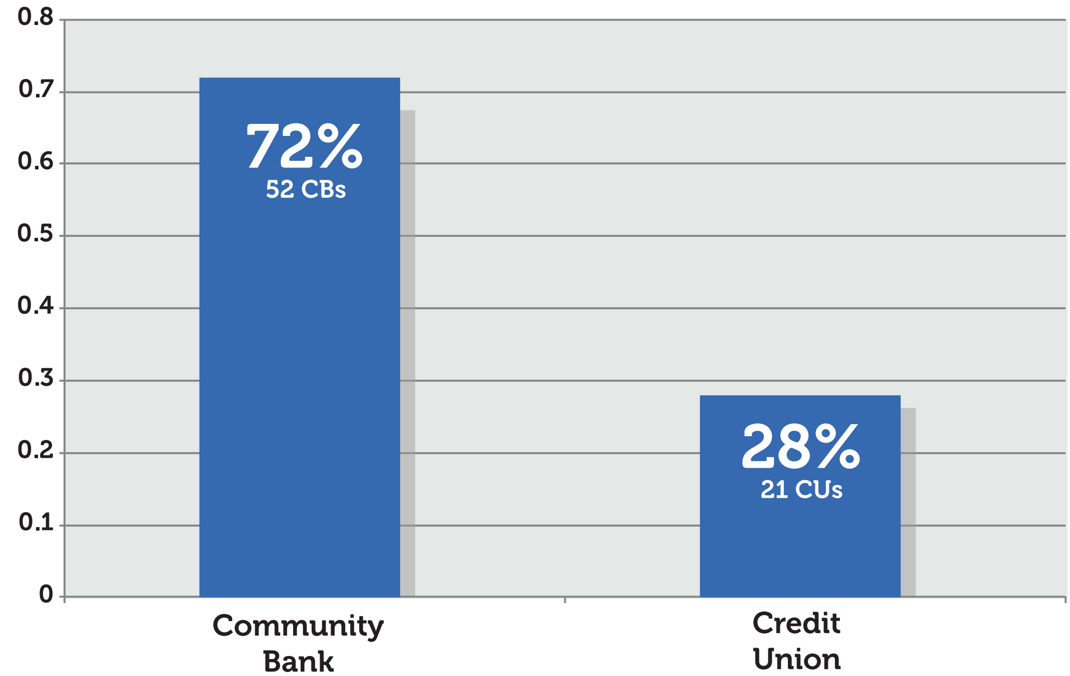
Methodology

A survey form was developed by the Florida Chamber Foundation for the *2012 Small Business Lending Survey*. Surveys were sent electronically via email to senior management staff of all community banks (locally owned depository institutions) and credit unions (not-for-profit financial cooperatives) headquartered in Florida with recorded total assets of $5 billion or less in 2011. The use of e-mail solicitation was the primary method for acquiring responses, which were collected through a web-based survey platform.

A total of 336 institutions were identified and sent surveys between June 15, 2012 and August 10, 2012. Of the 336 potential responding institutions, 75 institutions completed the survey, resulting in a response rate of 22.3 percent. The characteristics of survey respondents are closely aligned with the characteristics of institutions located in Florida (as described earlier), although the survey does not represent a random sample. Of those 75 institutions, 54 respondents were community banks (32% response rate amongst community banks contacted), and 21 respondents were credit unions (13% response rate amongst credit unions contacted). Amongst those community banks and credit unions that did complete the survey questionnaire, the median number of Full Time Equivalents (FTEs) was 37, and the median size of total assets was $210 million.

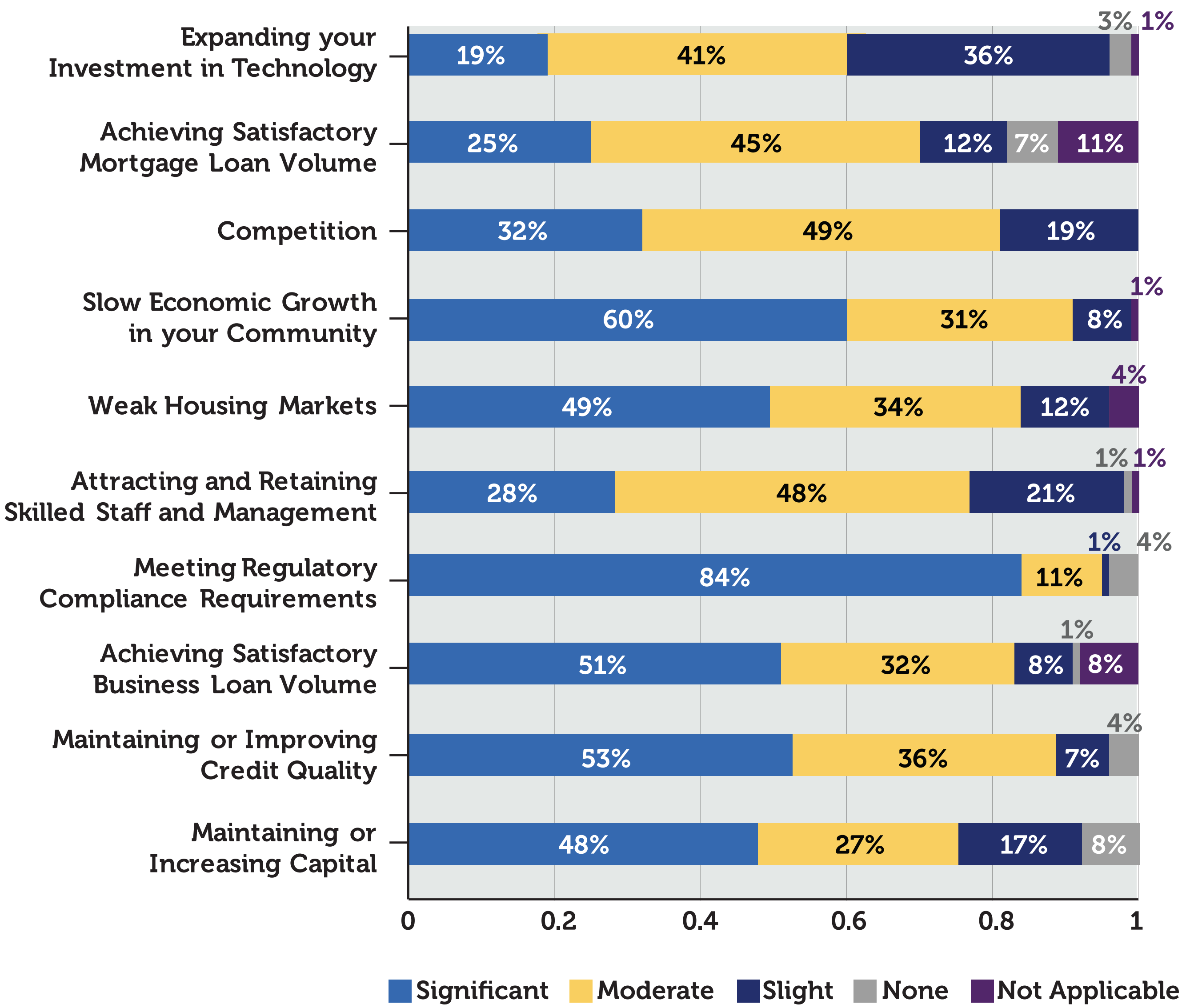
Appendix

Q1: What type of institution are you?

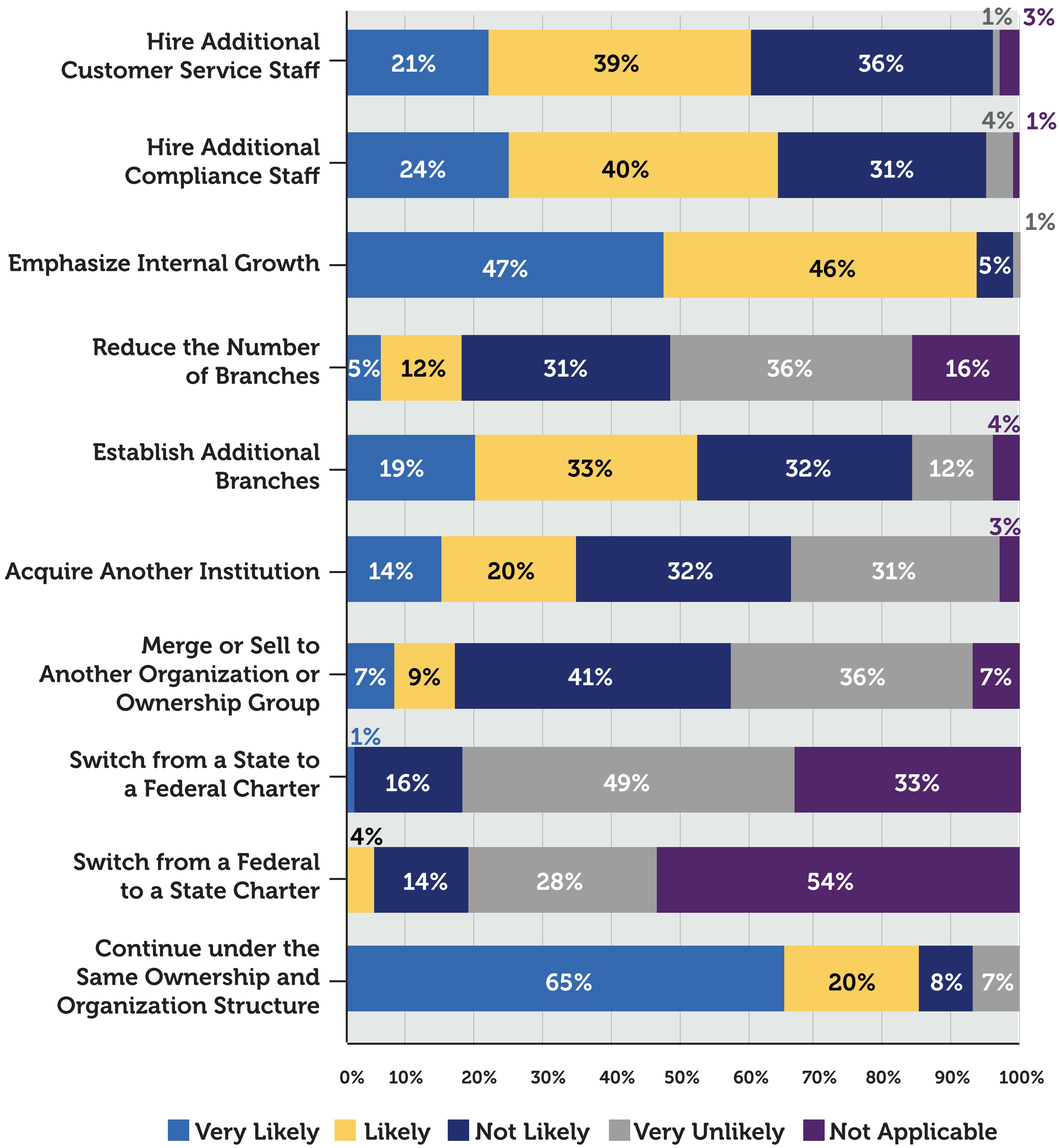


Questions 2-4 were optional and, thus, aggregate data cannot be provided here.

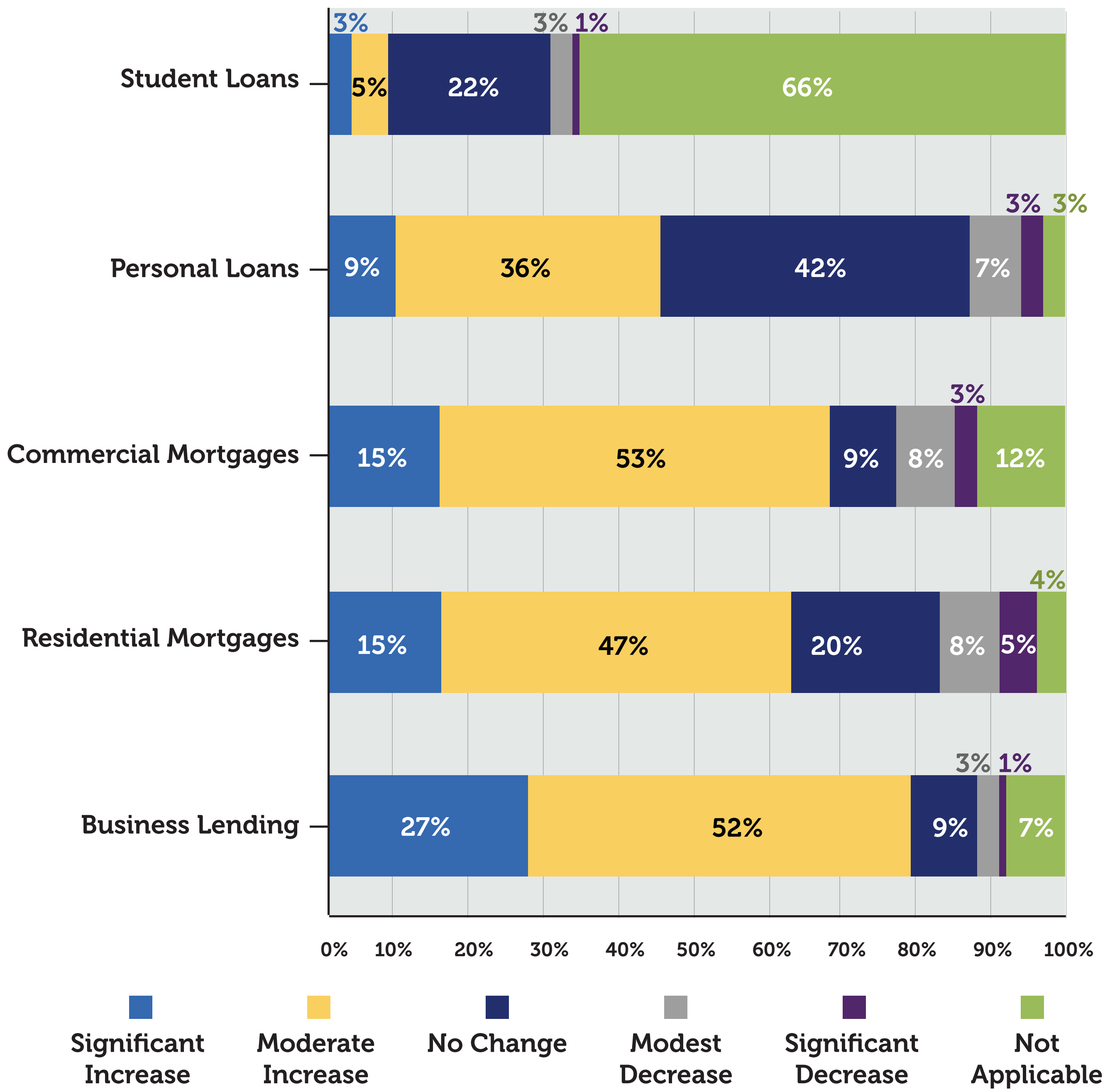
Q4: Rate the magnitude of strategic challenges you anticipate in the following areas over the next three years.



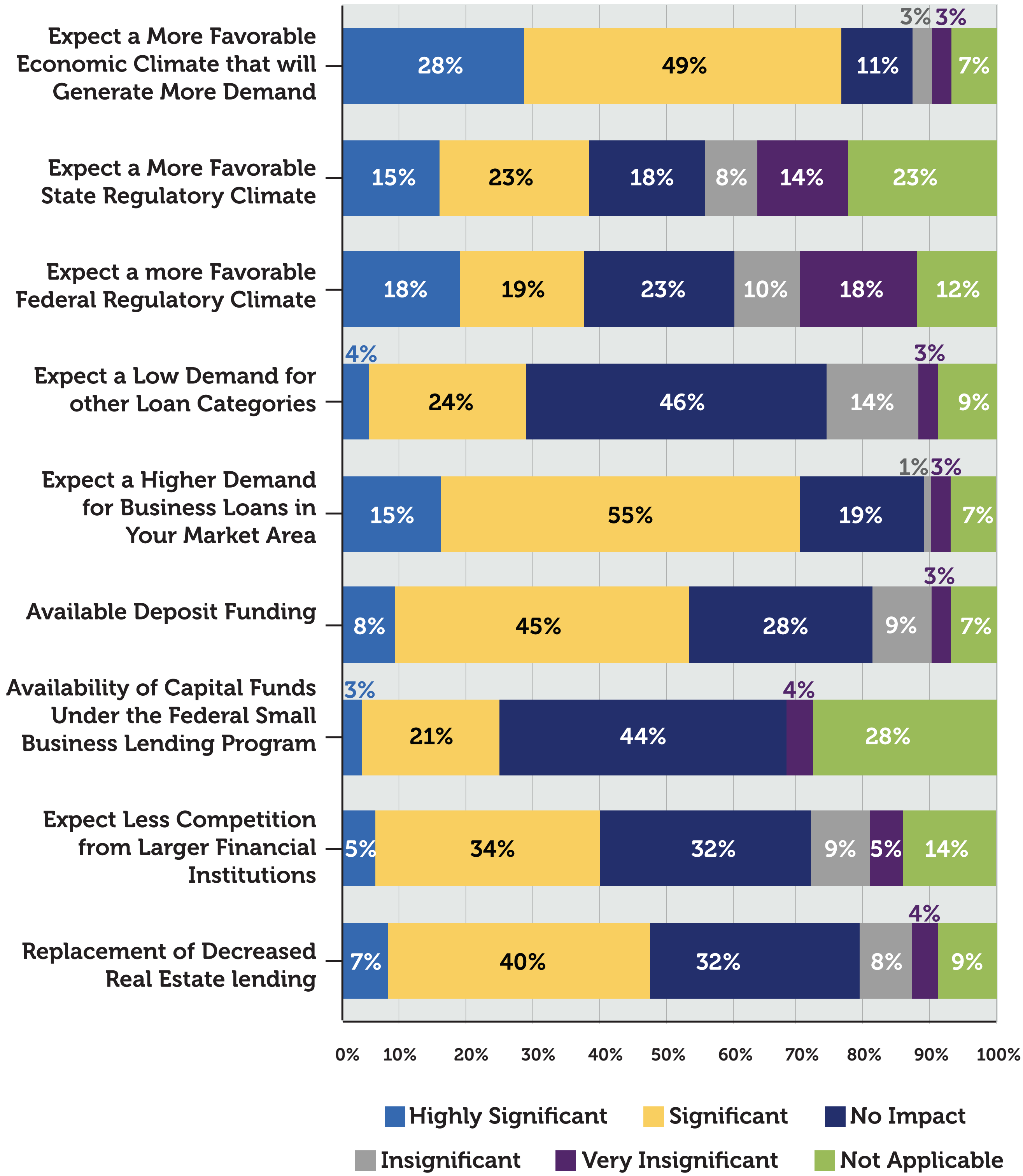
Q6: Over the next three years, your institution will:



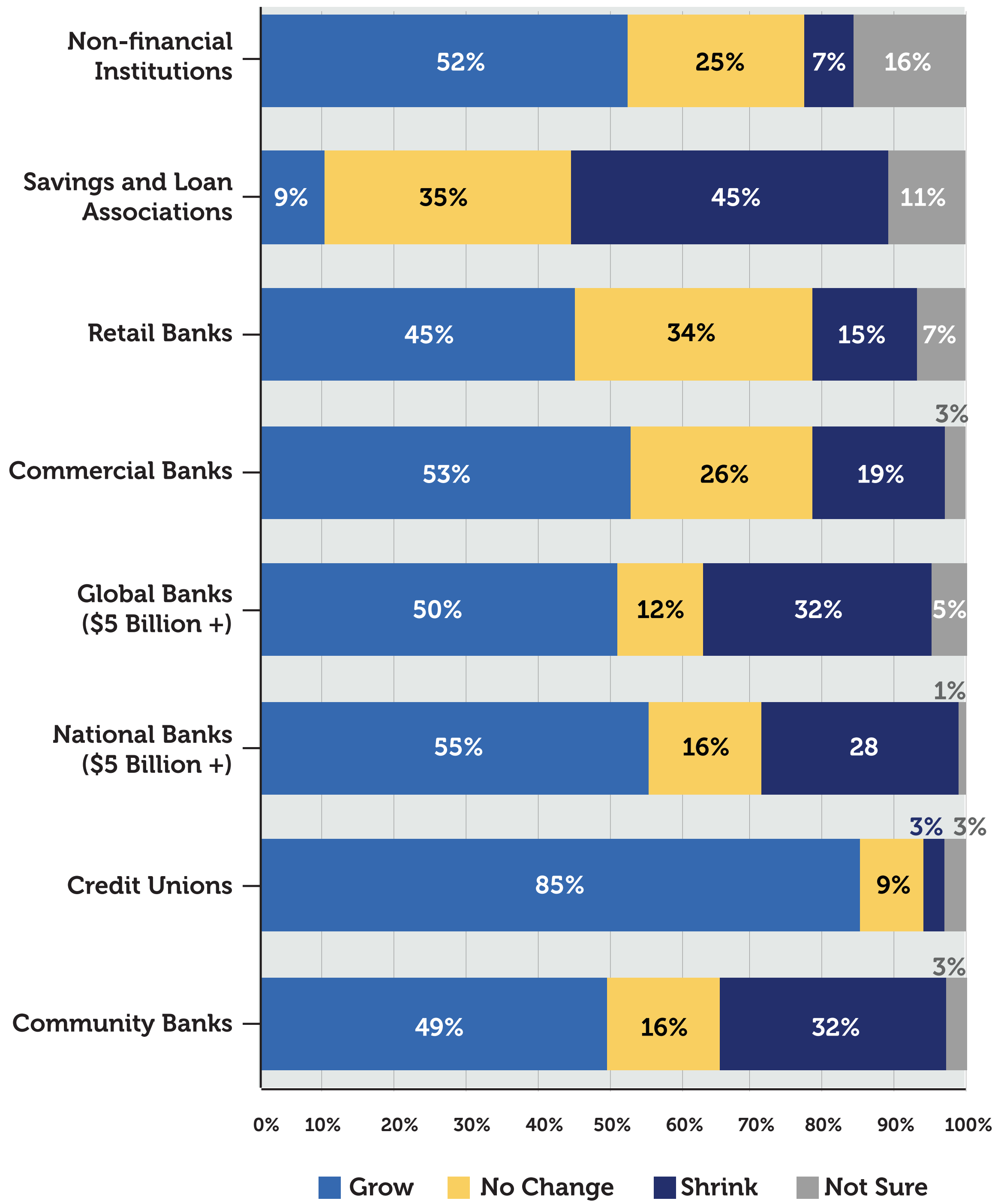
Q7: Of the following types of loans, what changes does your institution anticipate over the next three years?



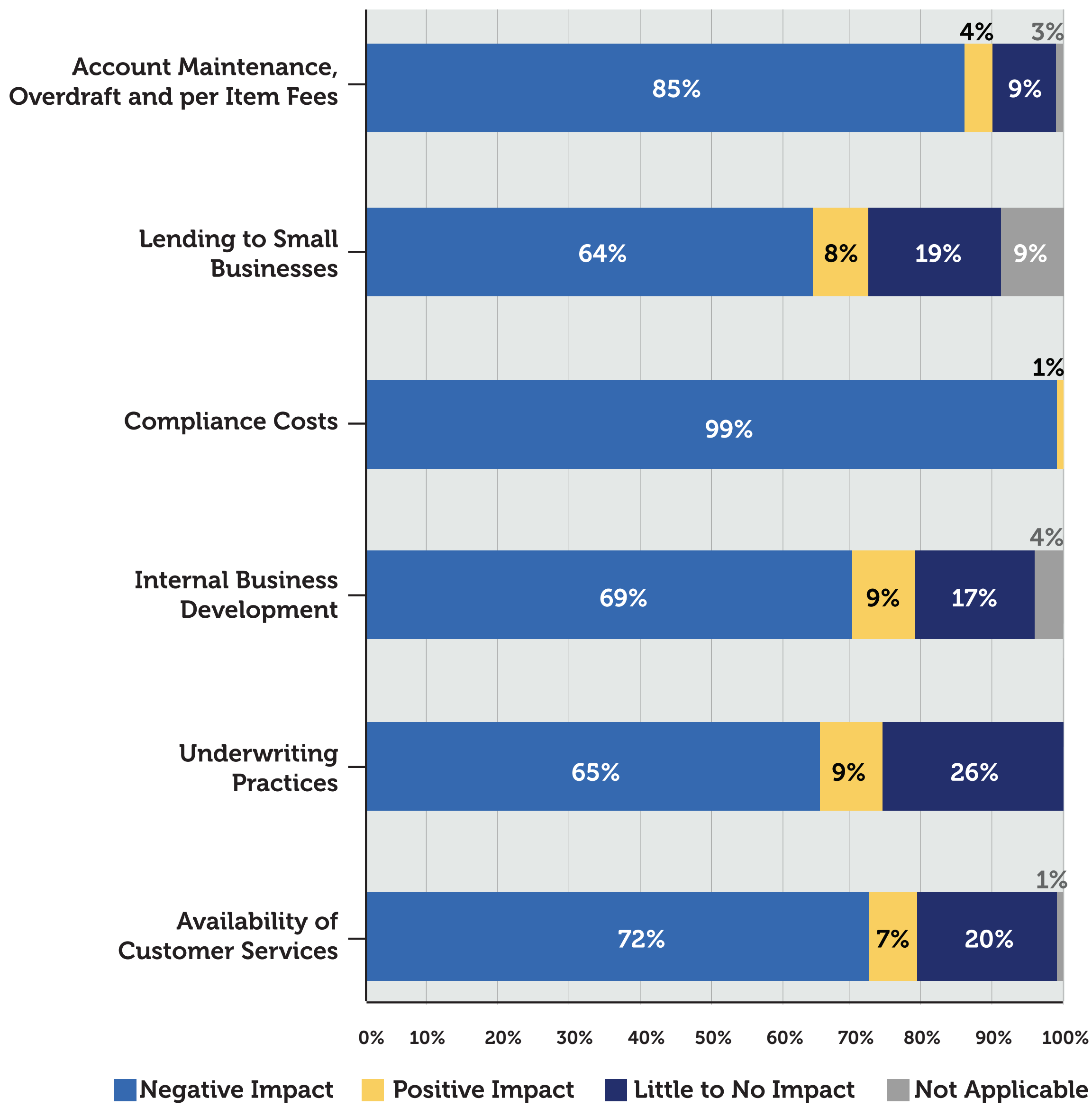
Q8: Rate the significance of the following factors in your institution's decision to increase business lending over the next three years:



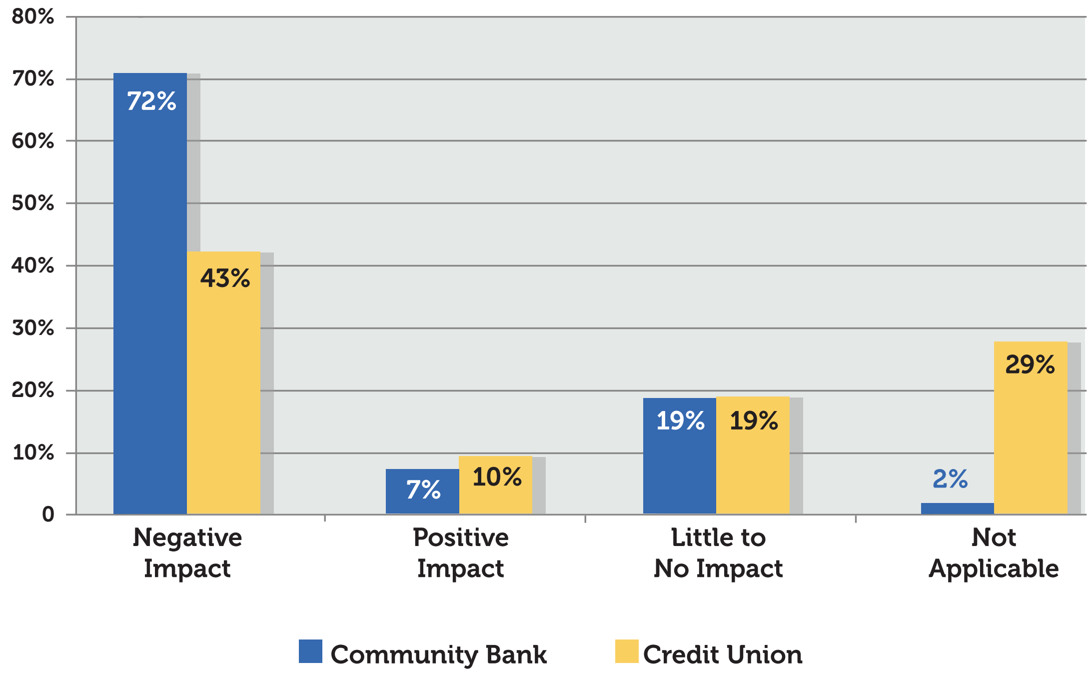
Q9: Based on your experience in the financial market place, how do you believe the following institutions will change in terms of total assets over the next three years?



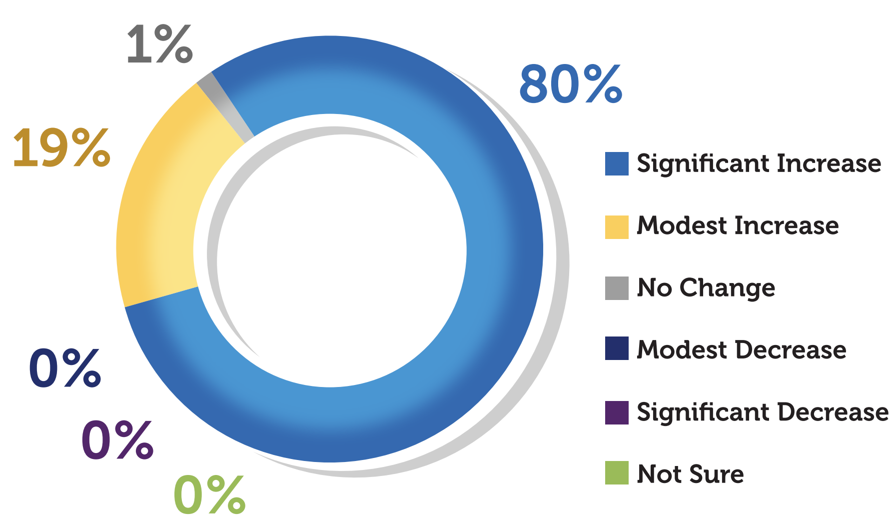
Q10: How do you expect the Dodd-Frank Act of 2010 to impact your institution over the next three years across the following areas?



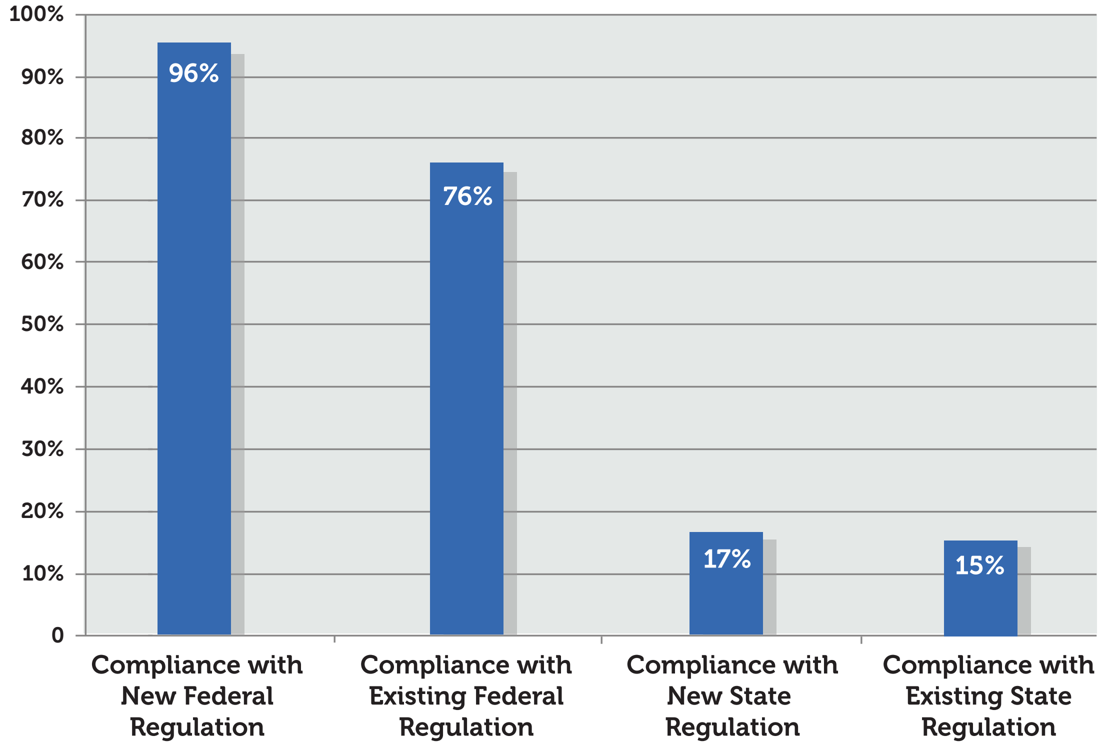
Q10 (a): How do you expect the Dodd-Frank Act of 2010 to impact your institution's small business lending over the next three years?



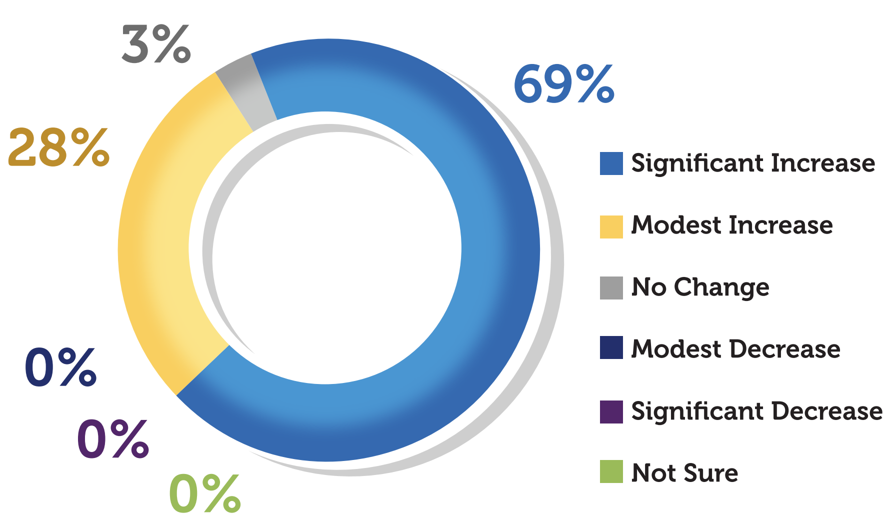
Q11: How do you expect that staff time and money spent on compliance issues will change over the next three years?



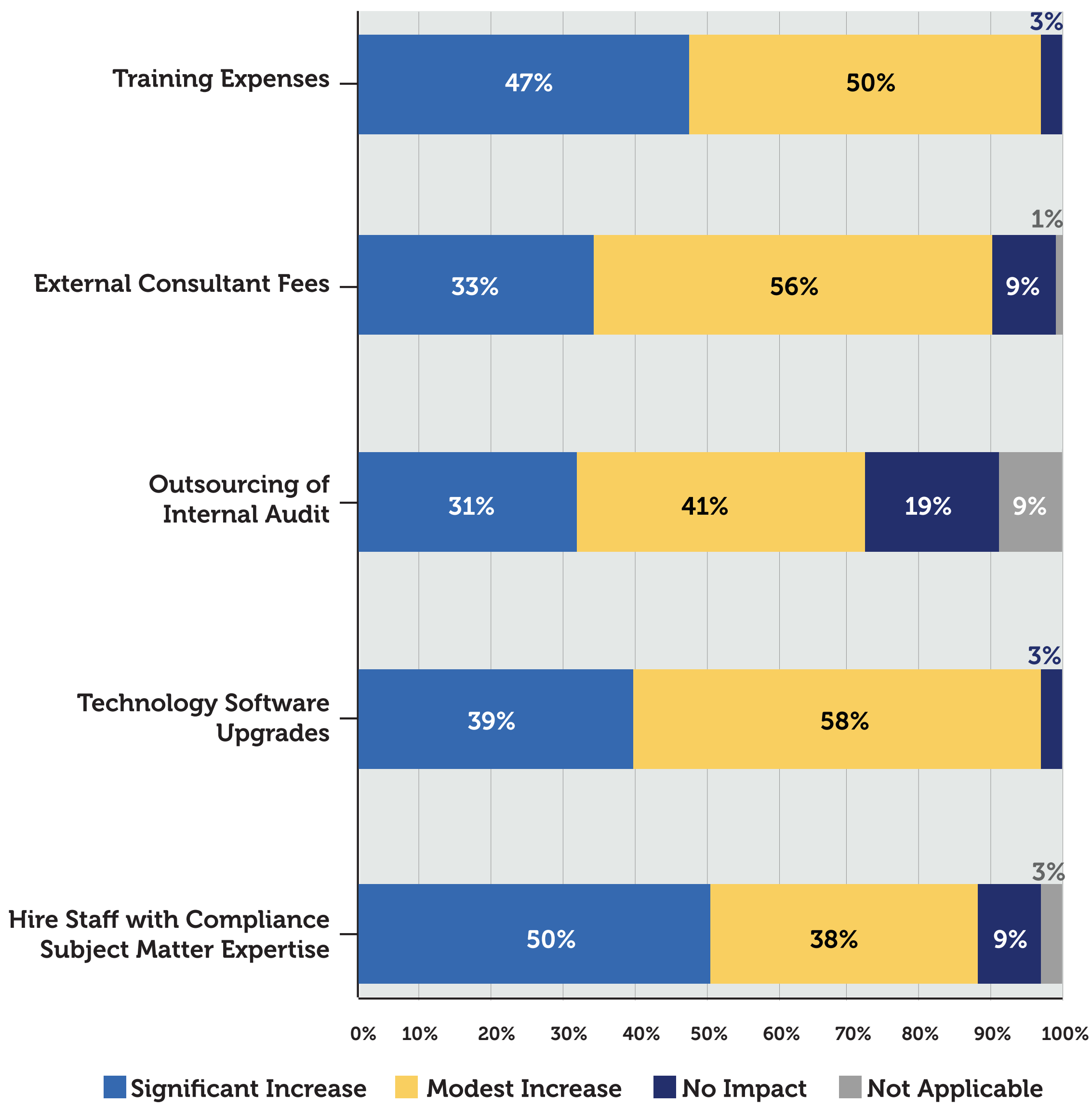
Q12: In which of the following compliance related areas do you expect to spend considerably more time and/or money over the next three years? (check all that apply)



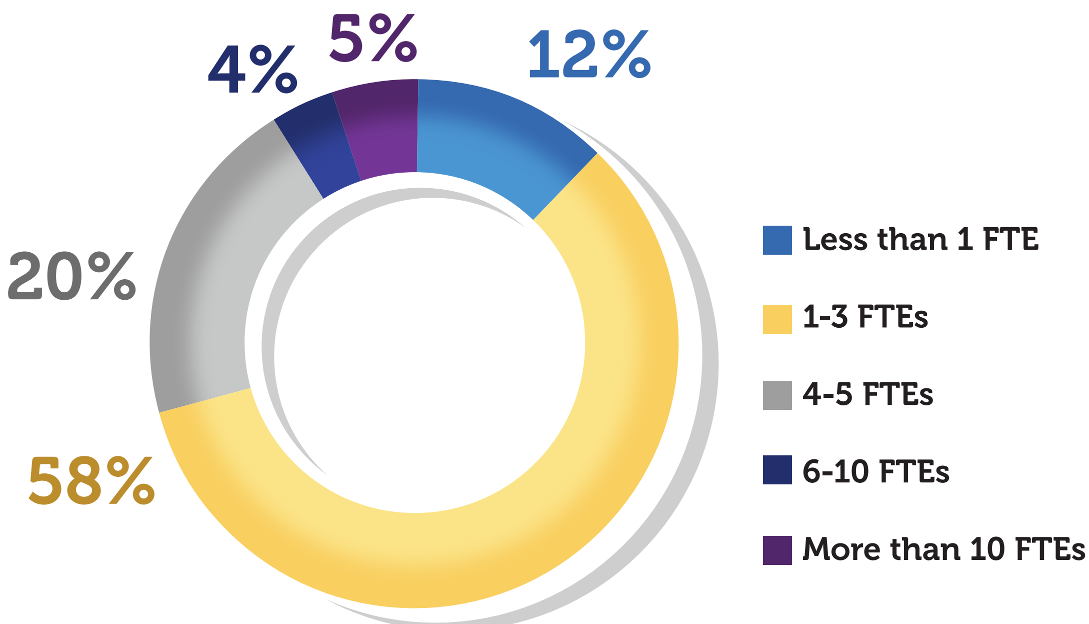
Q13: How will your senior management and Board of Directors' attention to compliance and resource planning change over the next three years?



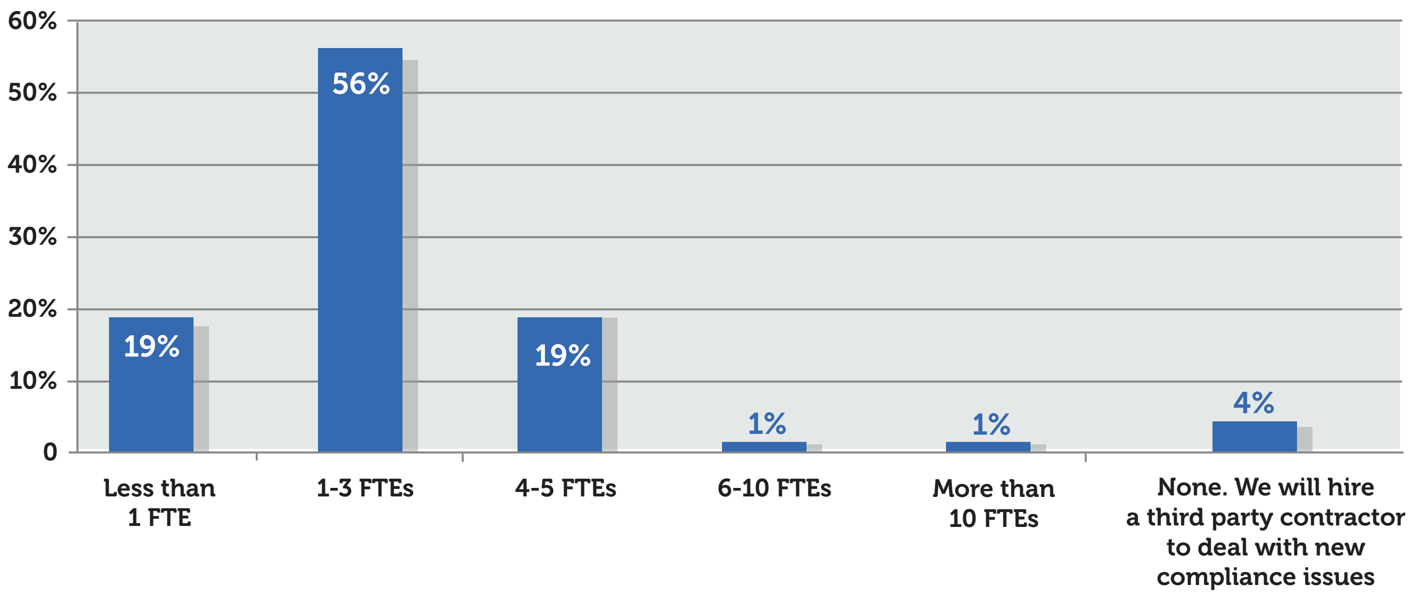
Q14: Estimate the budget impact of each of the following compliance management strategies for your institution over the next three years:



Q15: Indicate how many full time equivalent (FTE) employees are currently devoted to compliance at your institution:



Q16: Indicate how many additional full time equivalent (FTE) employees you expect to devote to compliance over the next three years:



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