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Industrial and Commercial Loans and Guarantees for New or Expanding Business Under the Public Works and Economic Development Act of 1965

JAMES M. ROBERTS

In his pivotal primary victory over Hubert Humphrey, President John F. Kennedy pledged that he would lend vigorous assistance to the impoverished coal mining regions of West Virginia to alleviate their economic distress. In fulfillment of this pledge, Congress passed and President Kennedy signed into law in May, 1961, the Area Redevelopment Act in order to "establish an effective program to alleviate conditions of substantial and persistent unemployment and underemployment in certain economically distressed areas."

The Area Redevelopment Act created an experimental pilot program within the Department of Commerce to accomplish the above purpose through a system of government loans for the establishment of new businesses or the expansion of existing firms; loans and grants to assist communities in providing needed public facilities for industrial expansion; technical assistance to communities; and job retraining. With the benefit of four years experience under the pilot program of this act, President Lyndon B. Johnson proposed on March 25, 1965, that a number of alterations be made in the Area Redevelopment Act and that the program be given permanent status for the purpose of carrying out the policies set forth in the act.

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Acting on the President's proposal, Congress considered and passed and the President on August 26, 1965, approved the Public Works and Economic Development Act of 1965. The act of 1965 replaces the Area Redevelopment Administration with the Economic Development Administration which continues as a part of the Department of Commerce under the authority of the Secretary of Commerce. Based generally upon the Area Redevelopment Act (Public Law 87-27), this act is also based to a certain extent upon the public works Acceleration Act (Public Law 87-658) and the Appalachian Regional Development Act (Public Law 89-4).

Recognizing that approval or disapproval of an industrial or commercial loan application will be conclusive of the creation or expansion of a business enterprise, and that approval holds the promise of increased activity and improved economic health of an entire area, the great importance of the procedure for making a loan application and the subsequent administrative determination relative to the application is readily apparent. It is, therefore, the purpose of this article to evaluate the alterations effected by the Public Works and Economic Development Act of 1965 with a consideration of past experience under the Area Redevelopment Act, and with particular consideration of the criteria and standards applicable in determining whether or not a business qualifies for a low interest rate industrial or commercial loan.

Area and District Eligibility for Assistance

In order to qualify for Economic Development Administration loan assistance, the new or expanded business project must be "within a redevelopment area." The act of 1965 provides that the Secretary of Commerce, under whose authority the Act is administered,

... shall designate as 'redevelopment areas'—(1) those areas in which he determines . . . there has existed substantial and persistent unemployment . . . and those areas in which he determines there has been a substantial loss of population due to lack of employment opportunity.7

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5 For an historical background of these three acts, see 2 U.S. Code Cong. & Ad. News 2790-92, 89th Cong., 1st Sess. (1965).
In designating redevelopment areas in accordance with the unemployment provision of the act, the Secretary must rely upon statistics furnished by the Secretary of Labor which must indicate that unemployment in the area is at least six per cent, and has averaged from fifty to one hundred percent above the national average for a stated period of preceding calendar years. These standards set forth in the act of 1965 are identical to those of the expired Area Redevelopment Act. Provision is in fact made for the continuance of redevelopment area designation of those areas so designated under the Area Redevelopment Act on or after March 1, 1965.

An area which has suffered a substantial loss of population because it lacks employment opportunities may be designated as a redevelopment area. This aspect is wholly new with the act of 1965. Thus an area which does not qualify for designation on some other ground, may still qualify under this provision on the basis of available data and standards set by the Secretary of Commerce and the Economic Development Administration.

Section 401 of the act of 1965 also provides that the Secretary of Commerce shall designate additional redevelopment areas under the following standards:

(2) ... areas which have a median family income not in excess of 40 per centum of the national median....

(3) ... Federal or State Indian reservations or trust or restricted Indian-owned land areas which the Secretary ... determines manifest the greatest degree of economic distress on the basis of unemployment and income statistics and other appropriate evidence of economic underdevelopment;

(4) upon request of such areas, those additional areas in which the Secretary determines that the loss ... of a major source of employment has caused within three years prior to, or threatens to cause within three years after, the date of the request an unusual and abrupt rise in unemployment of such magnitude that the unemployment rate for the area at the time of the request exceeds the national average, or can reasonably be expected to exceed the national average, by 50 per centum or more unless assistance is provided ....

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* Ibid.
The above standards remove the wide range of discretion which was left to the Secretary and the Area Redevelopment Administration under the Area Redevelopment Act. In accordance with its provisions, additional redevelopment areas (including Indian reservations) were designated which were determined to be "among the highest in numbers and percentages of low-income families" and included "a condition of substantial and persistent unemployment or underemployment." Finally, section 401 (4) of the act of 1965 adds as a basis for redevelopment area designation that due to a sudden loss of employment an area may be anticipated as becoming eligible for designation.

The determination that an area is qualified for designation does not create automatic eligibility for participation in the programs of the Economic Development Administration. In order to obtain official designation under the act of 1965, a qualified area must request such designation and obtain approval by the Secretary and Economic Development Administration of an overall economic development program (OEDP). The OEDP is a locally conceived area or community plan of action for the alleviation of conditions of unemployment and underemployment through the economic development of the area. The OEDP will generally contain the following analysis and evaluations leading to a plan of action for the area:

(1) a description of the representative local organization responsible for the overall economic development program;
(2) the background of the particular redevelopment area as a place to live and work;
(3) assessments of the labor skills, natural resources, physical facilities, transportation networks and available markets;
(4) some analysis of the difficulties and problems hindering economic progress, and
(5) some program of action for creating new employment and economic improvements.

The group of persons making the overall economic development program for a particular redevelopment area will include represen-

tatives from the major community interests—professional, business, labor, education, banking, agriculture, local government and others. In accordance with the provided procedure, the local committee first submits its OEDP to the state agency which has been designated by the governor to coordinate redevelopment activities in the state. It is then transmitted to the Economic Development Administration in Washington for review and approval. The requirement of the submission of an acceptable OEDP is the means chosen to implement the congressional policy of encouraging communities to take the initiative in their own economic development. It is generally thought within the Economic Development Administration—and justifiably so—that the stimulation of community and area economic planning is the most successful part of the program.

Section 401 (b) of the act of 1965, as well as containing the OEDP requirement, also specifies that redevelopment areas must have at least 1,500 persons, except Indian reservations, which need only 1,000 persons to qualify for designation. A final limitation relative to size applies to all areas except Indian reservations and areas requesting designation due to the loss of a major source of employment. Under this limitation no area is designated as a redevelopment area which is smaller than a county or a municipality of over 250,000 population or a "labor area" as defined by the Secretary of Labor. A labor area, as determined by the Secretary of Labor, is an economically integrated, primarily urban, geographical unit within which workers may readily change jobs without changing their place of residence.

Under the provisions of section 402 of the act of 1965, a redevelopment area's designation may be terminated with thirty days notice, if due to a permanent improvement in its employment and economic condition or a failure to maintain a currently approved overall economic development program, the area ceases to be eligible for such designation. This is subject to the exception,

16 Supra note 14.
however, that every state is entitled to at least one designated redevelopment area. Thus, termination is not permitted if to do so would result in the particular state having no designated redevelopment area. If no area qualifies for designation within a state, then the act of 1965 directs the Secretary of Commerce to designate as a redevelopment area, that area of the state which most nearly qualifies for designation.\textsuperscript{21}

The act of 1965 provides that those areas designated as redevelopment areas under the Area Redevelopment Act on or after March 1, 1965, should be initially designated redevelopment areas under the act of 1965.\textsuperscript{22} Upon request the Economic Development Administration will furnish a current list of the counties, labor areas, cities of 250,000 or more, areas suffering severe population losses, and Indian reservations which are qualified to participate in the programs provided by the Public Works and Economic Development Act of 1965. Among the states, West Virginia and Alaska have the highest percentage of counties which have been designated redevelopment areas eligible to participate in the programs provided by the act of 1965.\textsuperscript{23}

Under the Area Redevelopment Act, the usual designation of a redevelopment area followed the political boundaries of the county. Although this will continue to be the basic unit of designated redevelopment areas under the act of 1965, experience with the Area Redevelopment Act indicated that counties could often be advantageously grouped together to solve problems of mutual economic interest.\textsuperscript{24} Therefore, the Public Works and Economic Development Act of 1965 provides for the formation of "economic development districts" containing two or more redevelopment areas and at least one "economic development center" or redevelopment area "... having sufficient size and potential to foster the economic growth activities necessary to alleviate the distress of the redevelopment areas within the district."\textsuperscript{25} Economic development districts may extend across state boundaries, and the district boundaries

\textsuperscript{24} Supra note 14.
must be approved by the state or states involved. The economic development district must submit an overall economic development program for approval in the same manner as the individual re-development areas.  

The act of 1965 also authorizes the Secretary of Commerce to designate "economic development regions" consisting of parts of two or more states (with the exception of Alaska and Hawaii) when there is a geographic, cultural, historic and economic relationship between the region's areas and there is evidence sufficient to sustain a finding that the region has lagged behind the nation economically with respect to employment levels, family income, housing, health and educational facilities, dominance by one or two declining industries, labor and capital migration patterns, industrial technology and production. Under section 502 of the act of 1965, the states involved in the designated economic development regions will be encouraged to establish appropriate multi-state regional commissions. In carrying out the purposes of the act of 1965, these commissions are to advise and assist the Secretary of Commerce in determining the boundaries of the region, initiating and coordinating long-range overall economic development programs, fostering surveys and studies, initiating and coordinating economic development districts, promoting private investment, preparing legislation and developing plans.

Assistance to designated economic development regional commissions is limited to the financial costs of administrative and planning functions and technical assistance to aid in the development of recommendations and programs. No funds for development programs are provided, but redevelopment areas and economic development districts included in a specific region are eligible for assistance.

The above provisions of the Public Works and Economic Development Act of 1965 concentrate on the needs of larger economically viable distressed regions as a whole as well as the individual needs

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of the counties and communities of the larger region. This will make possible the planning of broad longer-range programs to alleviate the economic difficulties which the counties and communities of a region have in common. One of the weaknesses of the Area Redevelopment Act was its failure to provide for such long-range planning of programs on a regional and district scale.

Another difficulty encountered in the administration of the Area Redevelopment Act was the frequency of poorly prepared overall economic development programs due to the fact that few OEDP committees had the needed technical and economic knowledge to prepare a really adequate OEDP. Further, past OEDP's tended to be completely local in character, thus failing to take into consideration the needs of the larger economically depressed district or region of which it as a community or county might be only a small part.30 The act of 1965 will relieve these difficulties by providing technical assistance and encouraging the formation of development organizations large enough to employ trained technical people to prepare comprehensive plans of economic development.31

GRANTS AND LOANS FOR PUBLIC WORKS AND DEVELOPMENT FACILITIES

The Public Works and Economic Development Act of 1965 provides for grants and loans for development facility projects in redevelopment areas if they are either directly or indirectly related to the establishment of new industry. The act of 1965 authorizes grants of up to fifty per cent for development facility projects with grants of up to a total of eighty per cent of the cost of the project being allowed in severely distressed areas.32 Loans of up to one hundred per cent for development facility projects may be made where funds are not otherwise available from private lenders or from other federal agencies on terms which would permit the accomplishment of the project. In addition, there must be a reasonable expectation of repayment over a maximum duration of forty years.33 The interest rate charged for these loans is based on government borrowing cost less not more than one-half per cent.

30 Interview with Area Redevelopment Administration officials in Denver, Colorado, July, 1964.
The current interest rate charged is three and five-eighths (3\%) per cent annually.\textsuperscript{34}

Under section 202 (a) of the act of 1965, the Secretary of Commerce

\ldots is authorized (1) to purchase evidences of indebtedness and to make loans \ldots to aid in financing any project within a redevelopment area for the purchase or development of land and facilities (including machinery and equipment) for industrial or commercial usage \ldots and (2) to guarantee loans for working capital made to private borrowers by private lending institutions in connection with projects in redevelopment areas assisted under subsection (a) (1) \ldots \textit{Provided, however}, That no such guarantee shall at any time exceed 90 per centum of the amount of the outstanding unpaid balance of such loan.\textsuperscript{35}

The industrial and commercial loans and guarantees available to private businesses for facilities and working capital are subject to a number of restrictions contained in subsection (b) of section 202 of the act of 1965. Financial assistance will not be extended to assist businesses in relocating from one area to another or to assist businesses whose success depends upon their divestment of contracts from other businesses. However, assistance may be given for the expansion of an existing business through the establishment of a branch, affiliate or subsidiary if it is not being established with the intention of closing down an existing operation of the business.\textsuperscript{36}

The designated state agency concerned with economic development in the state where the proposed project would be located must approve the financial assistance. The project must also provide more than temporary alleviation of unemployment or underemployment.\textsuperscript{37}


The financial assistance requested must not be otherwise available from private lenders or from other federal agencies on terms which would permit the accomplishment of the project and, if possible, a requested loan will be made on a participation basis with other lenders. No loan or guarantee will be made unless there is a reasonable assurance of repayment within twenty-five years, and no evidences of indebtedness will be purchased which mature more than twenty-five years from the date of purchase.\textsuperscript{38} The loans and evidences of indebtedness provided are to be made at a rate of interest based on the government borrowing cost, which is currently four and one-eighth (4\%) per cent annually.\textsuperscript{39}

The act of 1965 provides for loan assistance of up to sixty-five per cent of the aggregate cost of the proposed industrial or commercial project, including the cost of acquiring or developing land and facilities. The loan requested is conditional upon the availability of other funds sufficient to cover the remaining aggregate cost. At least fifteen per cent of the aggregate cost must be furnished as equity capital or loan repayable at no faster a rate of amortization than the Economic Development Administration loan, and, if such loan is secured, its security must be subordinate to any lien securing the Administration’s loan. At least five per cent of the above fifteen per cent must ordinarily be supplied by the state or by a nongovernmental community or area organization. This requirement may be waived, however, if because of economic distress in the area or for other good cause this part of such funds is not reasonably available, in which case the applicant or some other non-federal source may supply the five per cent. Finally, except as to the above fifteen per cent requirement, the Secretary of Commerce may to the extent he finds such action necessary to encourage financial participation by other lenders and investors, take a subordinate lien to such other loans and permit repayment of the Administration’s loan after such other loans have been repaid in full.\textsuperscript{40}

Applications for Economic Development Administration commercial or industrial loan assistance are submitted on Form EDA-


\textsuperscript{39} See Pub. L. No. 89-136, § 202 (b) (8), 1 U.S. Code Cong. & Ad. News 615, 89th Cong., 1st Sess. (1965) and House Comm. on Public Works, supra note 34.

201, which is designed to provide a basic outline of the planned new business or expansion. On the basis of the information provided in Form EDA-201, the Economic Development Administration makes a determination as to whether or not the proposed commercial or industrial project qualifies under the above statutory provisions and merits a detailed and more extensive study to determine the actual approval and processing of the requested loan.\(^{41}\)

The most difficult portions of Forms EDA-201 relate to the project cost and proposed financing. A typical industrial loan application with regard to these matters might appear as follows:

3. **Cost of Project (Do not include working capital)**

   For the purchase or acquisition of:

   a. Land (attach plat)___________________________ $34,000
   b. Buildings (attach plan and cost estimates)_____ 396,000
   c. Machinery and equipment (attach itemized separate schedule and cost estimates)________ 3,020,000
   d. Other (Itemize) (Exclude organizational and promotional fees)___________________________ 548,000
   e. Contingency ______________________________ 62,000
   f. Total ______________________________________ $4,060,000

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<th>% of Project Cost</th>
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4. **Proposed Financing**

   a. EDA (Maximum 65%)____ 50% 12 4% $2,030,000
   b. Banks __________________ 20% 10 8 812,000
   c. Other private (Insurance Company, etc.)_______ 10% 12 8 406,000
   d. State or local development organization (Minimum 5%)_______ 5% 12 6 $203,000
   e. Equity's contribution or loan (Non-government source) 15% 609,000
   f. Other ________________________
   g. Total aggregate cost (should agree with Total of Item 3)_______100% $4,060,000

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\(^{41}\) Interview with Economic Development Administration Field Coordinator in Montgomery, Alabama, Dec. 20, 1965.
5. **Working Capital**
   
a. Borrowers funds .................................. $641,000  
b. Loans (Indicate source) .......................... 600,000  
c. Other sources ......................................  

Total .................................................................. $1,241,000\(^{42}\)

If the loan application is for an established business with operations in other locations, the applicant for a loan must include a certificate of non-relocation\(^{43}\) with his application. The applicant also must include a signed agreement to execute an assurance of compliance with the Department of Commerce regulations under Title VI of the Civil Rights Act of 1964\(^{44}\) as a prerequisite to final approval by the government of the accompanying application for financial assistance. Finally, the application must include a statement of the personal history of the proprietor (owner) if the applicant is a sole proprietorship, or by each general and each limited partner if the applicant is a partnership, or by each officer, director and stockholder holding twenty per cent or more of the applicant's voting stock, if the applicant is a corporation.\(^{45}\)

Section 202 (b) (10) of the act of 1965 includes the general requirement that an overall program for the economic development of the area be submitted and approved by the Secretary of Commerce, as well as a requirement that a finding by the state or local political subdivision thereof be made, as to whether the project for which financial assistance is sought is consistent with such program. This section also provides that no financial assistance shall be provided for any project prohibited by the laws of the state or the local political subdivision in which the project would be located.\(^{46}\) These requirements are included in the application for a commercial or industrial loan by a certificate of approval to

\(^{42}\) See, U. S. Dep't of Commerce, Economic Development Administration, Form EDA-201, Application for Commercial or Industrial Loan (Under Section 202 of Public Law 89-136) 1-2 (1965).


\(^{44}\) U. S. Dep't of Commerce, Economic Development Administration, Form EDA-502, Agreement to Execute an Assurance of Compliance with the Department of Commerce Regulations Under Title VI of the Civil Rights Act of 1964 (1965).

\(^{45}\) U. S. Dep't of Commerce, Economic Development Administration, Form EDA-201, Supplement I, Application for Loan Statement of Personal History (1965).

be executed by the officers of the state agency concerned with economic development and by the local OEDP committee of the area. These officers must certify that they have considered the proposed project and found it to be consistent with the approved overall program for the economic development of the area and that it is not prohibited by the laws of the state or local political subdivision in which it is located.\textsuperscript{47}

The above certification of the application for a commercial or industrial loan completes the formal application for loan assistance. The Field Coordinator of the Economic Development Administration will submit the application to the Washington, D. C. office along with his opinion of the proposed project for approval or disapproval. In its consideration, the Administration will include the economic feasibility of the proposed project, the amount of the government investment necessary, the economic impact that the proposed project may be expected to have on the area and whether or not the approval of the project would violate section 702 of the Act of 1965 which provides as follows:

No financial assistance under this Act shall be extended to any project when the result would be to increase the production of goods, materials, or commodities, or the availability of services or facilities, when there is not sufficient demand for such goods, material, commodities, services, or facilities, to employ the efficient capacity of existing competitive commercial or industrial enterprises.\textsuperscript{48}

It would be hard to find a proposed commercial or industrial project which would not compete with some existing business enterprise. The Economic Development Administration has made no policy or other interpretation of the above section of the act of 1965, but has decided to consider each application separately on a case by case basis.\textsuperscript{49}

If a proposed commercial or industrial project would create a locally owned business enterprise, this may be a factor in the Economic Development Administration's determination of approval of a loan application. Unfortunately, the Area Redevelopment

\textsuperscript{47} Supra note 42, at 5.
Administration did not give this important economic factor any significant consideration in its determination of approval or disapproval of loan applications. As an indication, however, that it is of some importance in the consideration of loan applications by the Economic Development Administration, is the following statement from a speech delivered by Mr. Eugene P. Foley, Economic Development Administration Director, at Concord College, Athens, West Virginia:

You need strong local business so that the money made in Southern West Virginia will be spent in Southern West Virginia; so that you will have a basis of strong business leadership to encourage outside firms to expand in your area; so there will be more jobs, more services, better quality goods for your people.

I know there is tremendous potential in an energetic local firm. With financial and management assistance, it can grow, prosper, and better an entire area.

The Area Redevelopment Act was primarily a job creation program whereas the Public Works and Economic Development Act of 1965 is more concerned with the economic stability and growth of depressed areas. Under the Area Redevelopment Act, great importance was placed upon the number of persons to be employed by a proposed project per dollar of Administration loan requested. This undoubtedly led to the approval of many projects which actually did little with regard to the economic stability and growth of the areas in which the projects were located. Under the same criterion, projects having a relatively high Administration loan investment per job created were denied loan assistance, although such projects could have made substantial contributions to the economic stability and growth of the designated redevelopment area.

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50 Interviews, supra notes 14 and 30.
51 Address by Assistant Secretary of Commerce and Economic Development Administration Director Eugene P. Foley at the Economic Development Conference at the Student Center of Concord College, Athens, West Virginia, Nov. 23, 1965.
52 Interviews, supra notes 14 and 30. The Area Redevelopment Administration adopted the unpublished rule of thumb for consideration of commercial and industrial loan applications, that it would not approve any loan application in which the Administration loan exceeded $20,000 per job created. This was later lowered to $10,000, and the more jobs a loan applicant could claim for his project per dollar of Administration money invested, the more likely was the project loan application to be approved.
Associated with the need for a dynamic locally owned industry is the fact that many areas suffer from the economic decline of some existing local industry. If the reason for the economic decline of that industry can be corrected, then the economic stability and growth of the designated redevelopment area will be restored. However, the declining industry may have no readily correctible economic difficulty, in which case the only alternative is the creation of new dynamic and locally owned industry. It may be noted that frequently in rural areas, where the local economy is dependent upon the success of the area's agricultural industry, the lack of economic stability and growth may be due to the need of a modern truck crop canning plant, a chemical nitrogen fertilizer plant, a quick-freeze potato processing plant or some other agriculture related industrial plant.

As above indicated, the act of 1965 places emphasis upon the economic factors responsible for the situation of a particular depressed area. This change in plan and emphasis of the congressional policy of providing assistance to depressed areas should greatly increase the long-range effectiveness of the economic development program. As President Johnson so well stated in his March 25, 1965, message to Congress:

The troubles and the potentials of depressed areas which contain approximately 27 million people vary widely. They are scattered across almost every section of the country . . . .

To restore vitality and forward motion to America's distressed areas, I recommend a program of area and regional economic development . . . .

In consideration of the alterations effected by the Public Works and Economic Development Act of 1965, it is apparent that it is an evolutionary improvement in almost every respect from the Area Redevelopment Act. Experience gained during the four years that the Area Redevelopment Act was in effect has shown that assisting businesses to expand or build new facilities is the most effective means of improving the economy of depressed areas. In West Virginia, the Area Redevelopment Administration approved eighteen industrial and commercial loans with a total value of $8,093,000. In the United States, the Area Redevelopment Administration ap-

53 Supra, note 31, at 5763.
proved 405 industrial and commercial loans with a total value of $176,143,000.\textsuperscript{44} Commercial and industrial project proposals approved by the Area Redevelopment Administration have included such facilities as a shoe factory, a fiberboard plant, a wood cabinet manufacturing plant, a plywood manufacturing plant, a ski area, a plastic products plant, a large motel, a green house company and the expansion and modernization of a small petroleum refinery.\textsuperscript{55} Probably none of these business enterprises and expansions could have become a reality in the redevelopment areas where they were located without depressed area industrial and commercial loan assistance.

In conclusion, it is apparent that industrial and commercial businesses locating in designated redevelopment areas will find the Economic Development Administration a promising source of investment capital not otherwise available. The additional possibility of obtaining a working capital guarantee is a further inducement to the business enterprise requesting an Administration loan. The low interest rate loans offered are difficult to obtain; however, the effort and preparation of the necessary loan application is well worthwhile for an enterprise which might otherwise be unable to obtain investment capital financing. The granting of such loans is also well worthwhile for the redevelopment area, the state and the United States as a whole since otherwise they will bear the hardship and loss, both human and economic, that is the national tragedy of the depressed areas.

\textsuperscript{44} U.S. DEP'T OF COMMERCE, AREA REDEVELOPMENT ADMINISTRATION, ANN. AND FINAL REPORT 15 (1965).
\textsuperscript{55} Interviews, supra notes 14 and 30.