



The Manufacturing Council

WASHINGTON, D.C. 20230

August 25, 2009

Dear Mr. Secretary,

Thank you for your leadership at the Department and for your recognition of the importance of manufacturing in America. As you know, in the current global economic crisis, small and medium sized manufacturing companies (SMMs) struggle to secure adequate lines of credit for basic day-to-day operations or investment in their facilities and employees. SMMs report significant segment discrimination by lenders – many impose prohibitive covenants or are no longer willing to work with manufacturing companies. Even under the strengthened Small Business Administration loan programs, lenders and manufacturers do not utilize them due to the stringent requirements and overly burdensome process. We ask for your immediate assistance in providing a bridge that assures economic prosperity for manufacturers in this great Nation.

Following a review of several hundred SMMs from around the country serving diverse industries, it remains clear that few financing options exist. In part due to fear of increased scrutiny from federal regulators, lending institutions repeatedly turn away long-established manufacturing companies. Until the federal government takes immediate steps to support SMMs, we expect a significant disruption in the critical supply chain across all industries, from national security to medical device production. Despite having a history of sound financial practices and profit margins, financial elements out of their control have caused many of these otherwise-healthy companies to become temporarily impaired.

While excessive lending to uncreditworthy entities is to blame for much of the current economic crisis, the pendulum has now swung to the extreme opposite – we need to rebalance our manufacturing financing system to open up credit to those SMMs that are traditionally healthy but temporarily impaired. We strongly believe that enforcing existing sound financing criteria, while ensuring that institutions no longer discriminate against healthy and temporarily impaired manufacturing companies, will open up lines of credit while mitigating risk to lenders and insulating taxpayers.

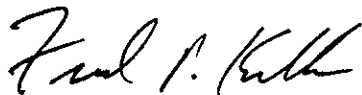
The Administration has the authority to assist SMMs by developing a program whereby the government will guarantee loans and/or receivables for domestic companies manufacturing in America. Under such a program, the primary source for repayment will remain the borrower, with the federal government only serving as a guarantor in the event of default. If proper and balanced criteria are enforced, lenders will return to providing sound loans to companies with reasonable expectations of repayment on terms. This will provide a level of comfort for lenders while ensuring the government, and taxpayers, are not overly exposed.

Mr. Secretary, inequitable treatment of small and medium sized companies manufacturing in America cannot continue. A significant bridge to allow these SMMs to continue daily production is essential to the nation's and the world's economic recovery. These are extraordinary circumstances that require immediate action and we cannot wait any longer for the manufacturing credit crisis to resolve itself. Lenders need a level of comfort to provide vitally needed credit for SMMs, and taxpayers need proper insulation from risk exposure, which will be accomplished through sound financing criteria.

On behalf of The Manufacturing Council, attached are several options to increase financing for SMMs. We offer ourselves as resources to you, as well as to Secretary Geithner, the National Economic Council, the Council of Economic Advisors, and any other agency you deem appropriate.

Thank you for continuing to work with us on this critical and urgent issue.

Sincerely,

A handwritten signature in black ink, appearing to read "Fred P. Keller". The signature is written in a cursive style with a large, prominent "F" and "K".

Fred Keller
Chair of the Council

Attachment

Government Guaranteed Loan, Accounts Receivable Sales, and Accounts Receivable Insurance Programs

Background

Manufacturers currently lack the access to credit to help finance their day-to-day operations, invest in expansion of domestic operations and ensure a disruption in the critical supply chain does not occur. Small and medium sized businesses¹ manufacturing (SMMs) in America continue to bear the brunt of the financial crisis – trapped between their customers and creditors. Traditional lenders have either drastically reduced lines of credit or denied loans to companies that are healthy or temporarily impaired due to the global economic crisis.

The federal government should step in and help ensure that domestic manufacturers continue to have access to credit and cash in order to continue supplying the nation's defense, medical, aerospace, automotive, and agriculture industries, among others. Due to the diverse nature of industries served and geographical locations of individual manufacturing companies, a federal one-size fits all approach may not be enough to address the unique needs of SMMs. Depending on a number of variables, some SMMs may be more suited to participate in a government-backed loan program, while others believe a program allowing them to guarantee their accounts receivable (A/R) through safe passage or an A/R sales program is more suited to meet their needs and those of their customers. The federal government should step in to help provide reliable and realistic standards and criteria to help support small and medium sized businesses manufacturing in America².

This proposal examines three concepts: loans, insurance for Accounts Receivable (A/R), and A/R sales, which will help manufacturers meet their unique needs while preventing a significant disruption in the critical supply chain.

Government Guaranteed Loan Program

While mechanisms currently exist within the federal government³ to provide financial support to healthy and temporarily impaired companies, there lacks a comprehensive manufacturing plan to ensure employers and employees have the financial resources they need to continue serving their customers. Despite well-intentioned government initiatives such as the Small Business Administration's 7(a) loan program, lenders continue to find that many manufacturers simply are not "bankable" under current conditions. Companies continue to struggle with unrealistic criteria and mandates under the SBA programs. For example, few manufacturing companies report utilization of SBA loan programs; estimates are that fewer than 5 percent of the overall industry which includes roughly 100,000 firms take part. While the majority of manufacturing firms believe an increase in the SBA loan cap limit is needed to make the program more attractive, the vast majority still believe the paperwork process combined with a personal guarantee cannot make an SBA loan attractive enough to pursue.

In the current economic environment, many manufacturing companies who are historically healthy are now temporarily impaired. These firms are critical in maintaining an uninterrupted supply chain but their traditional lenders will no longer extend a sufficient line of credit. Therefore, the federal government should step in and support manufacturing in America by providing a government guarantee for private lending to these business.

¹ An eligible company must meet the definition of a small business under the Small Business Administration's size standards matched to North American Industrial Classification System Codes (NAICS) (more than 98.6% of manufacturing companies have fewer than 500 employees).

Typically 500 or 750 employees - http://www.sba.gov/idc/groups/public/documents/sba_homepage/serv_sstd_tablepdf.pdf

² According to the Census Bureau, roughly 282,034 SMMs exist in the U.S. as of 2006.

³ Farm Credit Administration, a Government-Sponsored Enterprise created by Congress in 1916 to provide American agriculture with a dependable source of credit.

SMM Loan Facility Program

This legislation authorizes the Secretary of the Treasury to provide a government guarantee to companies using existing funds in the Term Asset-Backed Securities Loan Facility (TALF) program. Under TALF, the government will guarantee loans to domestic manufacturing companies of up to \$10 million on the following scale:

- 90% up to \$2.5 million whereas the bank assumes 5% of the risk and borrower 5% of risk.
- 80% up to \$5 million whereas the bank assumes 10% of the risk and borrower 10% of risk.
- 70% between \$5-10 million whereas the bank assumes 15% of the risk and borrower 15% of risk.

Loan Terms

Financial institutions shall provide loans under this program for term not to exceed three years and shall adjust in accordance with the prime interest rate. Pre-payment penalties shall not be applied.

Use of Loan Funds

Such loan is not used to pay down existing debt, pay outstanding obligations, or pay for building acquisition or construction other than facility improvements. Eligible uses include:

- paying payroll expenses
- working capital
- productivity enhancements
- energy efficiency
- operating costs (to include utilities, taxes, etc.)
- tooling, new equipment, and material purchase

Loan Evaluation Criteria

Under this program a financial institution cannot deny a loan because a company is temporarily impaired due to the global economic crisis. A financial institution may refuse credit to a firm that is "Other Than Temporarily Impaired" (OTTI)⁴. Companies that are considered healthy or temporarily impaired must present to the lender a plan that shows historical financial and market strengths, be impaired solely by market or economic conditions and not their own competitive standing, and can demonstrate future success defined as:

- Future business booking through proof of a purchase order (PO);
- A positive cash flow within twelve months;
- A demonstrated ability to cover the guarantee as set forth in the above schedule.

Financial Institution Participation

Financial institutions that participate in this program shall not have any of these loans account negatively against their ratings as determined by the Office of the Comptroller of the Currency (OCC) or any other federal or state regulatory entity.

Loan Funding

In general, \$20,000,000,000⁵ shall be made available until expended under the Term Asset-Backed Securities Loan Facility (TALF) program or related successor entity. The program shall expire on December 31, 2010 unless extended through notification of the Congress by the President.

Government Guaranteed Accounts Receivable (A/R) Sales Program

Uncertainty surrounding the timeliness of paid receivables and a need for a steady cash flow for day-to-day operations and investments creates challenges for these critical supply chain manufacturers.

⁴ This Federal Accounting Standards Board (FASB) Staff Position (FSP) addresses the determination as to when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. When an investor has decided to sell an impaired available-for-sale security and the investor does not expect the fair value of the security to fully recover prior to the expected time of sale, the security shall be deemed other-than-temporarily impaired in the period in which the decision to sell is made.

⁵ According to the Census Bureau, roughly 282,034 SMMs exist in the U.S. as of 2006.

Traditional lenders remain concerned about the health of a manufacturing company's customers, meaning the ability to collect on accounts receivable. For example, a majority of manufacturing companies believe a government-backed private accounts receivable financing program will inject immediate cash into the business through the sale of their receivables to a private third party entity and would help these critical suppliers weather the economic storm⁶.

Establishment of Program

The federal government would establish a program within the Department of Treasury for a government-backed private accounts receivable financing system for domestic small and medium sized manufacturing companies. This will allow companies to secure immediate cash flow through the sale of their A/R in a process also known as "factoring"⁷ - currently a \$1 trillion global industry (\$100 billion in North America⁸). This legislation establishes a program where the federal government will guarantee 100% of receivables sold to a financial institution by eligible manufacturing companies.

Terms for A/R Program

If a financial institution purchases an A/R at full value, the government will guarantee 100% of that receivable. For this service, the institution may charge a fee not to exceed 1%.⁹ Should the institution be unable to collect the A/R, it shall pay the federal government a .5% fee to assume the outstanding A/R.

Funding for A/R Sales Program

In general, \$20,000,000,000¹⁰ shall be made available until expended under the Troubled Assets Relief Program (TARP) or related successor entity. The program shall expire on December 31, 2010 unless extended through notification of the Congress by the President.

Government Guaranteed Accounts Receivable Insurance Program

The government should create a program to provide safe passage of receivables for manufacturing companies. An Accounts Receivable Insurance (ARI) program, similar to one in existence in Canada, would insure receivables on a full book of business for 100% of losses against such commercial risks including but limited to:

- customer refusing to pay;
- refusal to accept the goods;
- bankruptcy or insolvency;
- cancellation of import or export permits;
- currency transfer;
- war, revolution, or insurrection; and
- contract cancellation.

ARI Guarantee

Manufacturing companies would secure their A/R through purchasing insurance from private companies for a fee not to exceed 1%.

Funding

The government shall hold in reserves \$20,000,000,000 from the Troubled Assets Relief Program (TARP) or related successor entity in order to secure the ARI.

⁶ Survey of manufacturing companies: 56% reported they would participate; 24% unsure; and 18% no.

⁷ Factoring - An arrangement in which a company shortens its cash cycle by selling its accounts receivable without recourse to a third party, known as a "factor." A factor assumes the full risk of collection, including credit losses. Factors frequently perform all accounting functions in connection with the accounts receivable, in which case purchasers are notified to remit payments directly to the factor. (*U.S. Comptroller of the Currency, "Accounts Receivable and Inventory Financing," Comptroller's Handbook, March 2000*).

⁸ "Ex-Exec Mends Cash Flow For Small Businesses," Canwest News Service, June 6, 2009.

⁹ Based on online reviews of several factoring companies, industry average is between a 2-3% fee for a 30-day invoice (account receivable).

¹⁰ According to the Census Bureau, roughly 282,034 SMMs exist in the U.S. as of 2006.