

36 Park Street
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Ref: L14874

6 April 2004

Dear Teresa Graham,

THE GRAHAM REVIEW OF THE SMALL FIRM LOAN GUARANTEE

The Federation of Small Businesses (FSB) welcomes the opportunity to comment on the above review on behalf of its 185,000 members.

Please find our comments in the document attached, which you will also receive shortly as a hard copy by post.

We trust that you will find our comments helpful and that they will be taken into consideration. The FSB is willing for this submission to be placed in the public domain. We would appreciate a copy of the synopsis of responses and of being kept fully informed of further developments on this issue.

Yours sincerely,

Reema Shah
0207 592 8106



**RESPONSE FROM THE
FEDERATION OF SMALL BUSINESSES (FSB)**

TO

The Graham Review of the Small Firms Loan Guarantee

FEDERATION OF SMALL BUSINESSES

The Federation of Small Businesses (FSB) is the UK's leading non-party political lobby organisation existing to promote and protect the interests of all who own and/or manage their own businesses in the UK. With over 185,000 members, the FSB is also the largest group representing the interests of UK small businesses and the self-employed.

Introduction

The FSB welcomes the opportunity to comment on the review of the Small Firms Loan Guarantee (SFLG). Whilst recognising that the recent changes made in relation to the SFLG, namely extending the scheme to new sectors such as child care and education, as well as raising the amount available to manufacturing businesses, will have a favourable impact on small businesses, the FSB believes that further reform is still needed.

Current problems with the SFLG

The FSB has found that many small businesses are unaware of the SFLG as bank staff and managers are reluctant to recommend it (particularly for smaller advances) due to the complexity of the application form, the time-consuming application process and the ongoing monitoring requirements (the need to obtain management accounts from the business and analyse them on a quarterly basis for the duration of the loan). Indeed, as the 2002 FSB survey "Lifting the Barriers to Growth in UK Small Businesses" shows, only 2.6% of the 18,500 respondents used the loan guarantee scheme as a source of finance. Translating that as representative of the totality of FSB membership, it means 4,625 FSB members used the SFLG that year.

Evidence shows that many businesses have to wait up to six months for an application to be successful, by which time they no longer need the loan. We welcome the proposal to raise the current £30,000 limit above which lending institutions must get approval from the SFLG unit of the Small Business Service (SBS), as this will speed up the process. However, the FSB recommends that the requirement for approval from the SFLG unit is completely removed for loans of all amounts.

Changes in banks' sanctioning procedures have in many cases, removed the discretion of local bank business managers to lend to small and micro businesses. Most lending decisions are made with credit scoring systems that do not always allow for all factors to be considered. It is quite possible that some viable businesses may be unable to get the finance they need due to inflexibilities of the credit scoring systems. The FSB believes that banks should seek alternative methods of deciding whether to issue a loan or not, based more on whether a business is self reliant and has potential for future development.

The FSB is concerned about the declining number of smaller loans (under £30,000) as a proportion of all loans. Recent evidence has found that businesses seeking as little as £30,000 face huge difficulties in obtaining loan finance. Furthermore, start-up companies find it increasingly difficult to find any source of external finance. The FSB questions whether this decline in smaller loans is due to the reluctance of bank staff to offer the SFLG to micro businesses with relatively low borrowing requirements.

FSB Recommendations

As a result of the low take-up of the scheme, the FSB recommends that a large-scale programme is required to raise awareness of the SFLG. This should be targeted at both the banks and the small business owners, in particular at micro business owners, whose lending requests are often dealt with by bank staff with little knowledge of alternative lending options to credit. The FSB has found that bank staff dealing with micro businesses may not have the knowledge or expertise to advise on specialist lending schemes such as the SFLG. Currently, there seems to be little incentive to encourage banks to invest time and money on training staff on the SFLG. The FSB therefore recommends that the relevant bank staff are trained on all aspects of the SFLG.

In addition, the FSB believes that the application process and paperwork should be simplified. Businesses have to complete DTI forms, as well as standard bank lending application forms. A review of the paperwork both by the DTI and the banks would be welcome.

The FSB supports broadening the lender base, to include, as the Review suggests, Community Development Finance Institutions, as well as other lending institutions that have not yet engaged in the scheme. We feel that this would provide a greater choice to businesses. The FSB would also like to see a similar initial application process for the SFLG amongst all the lending institutions in order to make the procedure simple for businesses.

Most importantly, we would like the lending institutions to have more control over issuing the loans. We feel the SBS should have limited control of the SFLG process, for example, by removing the requirement to obtain approval from the SFLG unit for loans of all amounts. The FSB feels that banks should be allowed to make decisions regarding the loan without constant consultation with the SBS.

Conclusion

The FSB supports the SFLG, in particular the recent changes made to the scheme but feels that it should be promoted proactively by the lending

institutions so that all businesses are aware of it. Furthermore, the process should be simplified with less reliance being placed on the SBS, which tends to slow down the application process. By giving more control to lending institutions to make decisions regarding the loan, the FSB feels the SFLG will be more accessible to small businesses and bank staff, following the relevant training, will be more enthusiastic to promote the loan.

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