



Small Business Administration 7(a) Loan Guaranty Program

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November 8, 2011

Congressional Research Service

7-5700

www.crs.gov

R41146

Summary

The Small Business Administration (SBA) administers several programs to support small businesses, including loan guaranty programs designed to encourage lenders to provide loans to small businesses “that might not otherwise obtain financing on reasonable terms and conditions.” The SBA’s 7(a) loan guaranty program is considered the agency’s flagship loan guaranty program. It is named from Section 7(a) of the Small Business Act of 1953 (P.L. 83-163, as amended), which authorized the SBA to provide business loans and loan guaranties to American small businesses. In FY2011, the SBA approved 53,706 7(a) loans amounting to more than \$19.6 billion.

Congressional interest in the 7(a) loan program has increased in recent years because of increased concern that small businesses might be prevented from accessing sufficient capital to enable them to assist in the economic recovery.

This report opens with a discussion of the rationale provided for the 7(a) program; the program’s borrower and lender eligibility standards and program requirements; and program statistics, including loan volume, loss rates, use of the proceeds, borrower satisfaction, and borrower demographics.

It then examines congressional action taken during the 111th Congress to help small businesses gain greater access to capital. For example, in 2009, P.L. 111-5, the American Recovery and Reinvestment Act of 2009 (ARRA), provided additional funding to temporarily subsidize the 7(a) program’s fees and to increase the program’s maximum loan guaranty percentage to 90%. In 2010, P.L. 111-240, the Small Business Jobs Act of 2010, provided additional funding to extend the 7(a) program’s fee subsidies and 90% maximum loan guaranty percentage through December 31, 2010; increased the program’s loan guaranty limit from \$2 million to \$5 million; and established an alternative size standard for the 7(a) and 504/CDC loan programs, which is designed to increase the number of small businesses that can participate in the two programs. Also, P.L. 111-322, the Continuing Appropriations and Surface Transportation Extensions Act, 2011, authorized the SBA to continue the fee subsidies and the 7(a) program’s 90% maximum loan guaranty percentage through March 4, 2011, or until available funding was exhausted (which occurred on January 3, 2011).

This report also examines issues raised concerning the SBA’s administration of the 7(a) program, including the oversight of 7(a) lenders and the program’s lack of outcome-based performance measures. It also provides information concerning the 7(a) program’s SBAExpress, Patriot Express, Small Loan Advantage, and Community Advantage programs.

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Small Business Administration Loan Guaranty Programs

The Small Business Administration (SBA) administers programs to support small businesses, including loan guaranty programs to encourage lenders to provide loans to small businesses “that might not otherwise obtain financing on reasonable terms and conditions.”¹ The SBA’s 7(a) loan guaranty program is considered the agency’s flagship loan program.² It is named from Section 7(a) of the Small Business Act of 1953 (P.L. 83-163, as amended), which authorizes the SBA to provide business loans to American small businesses. In FY2011, the SBA approved 53,706 7(a) loans amounting to more than \$19.6 billion.³

The SBA also administers several 7(a) subprograms that offer streamlined and expedited loan procedures for particular groups of borrowers, including the SBAExpress, Patriot Express, Small Loan Advantage, and Community Advantage Pilot programs (see the **Appendix** for additional details). Although these subprograms have their own distinguishing eligibility requirements, terms, and benefits, they operate under the 7(a) program’s authorization.⁴

Historically, one of the justifications presented for funding the SBA’s loan guaranty programs has been that small businesses can be at a disadvantage, compared with other businesses, when trying to obtain access to sufficient capital and credit.⁵ Congressional interest in the 7(a) loan program has increased in recent years because of increased concern that small businesses might be prevented from accessing sufficient capital to enable them to assist in the economic recovery. For example, senior loan officers at private lending institutions have indicated in Federal Reserve Board surveys that they have tightened small business lending standards, largely in reaction to relatively high loan default rates and increased numbers of noncurrent (past due) loans.⁶

¹ U.S. Small Business Administration, *Fiscal Year 2010 Congressional Budget Justification*, Washington, DC, p. 30.

² U.S. Congress, House Committee on Small Business, Subcommittee on Finance and Tax, *Subcommittee Hearing on Improving the SBA’s Access to Capital Programs for Our Nation’s Small Business*, 110th Cong., 2nd sess., March 5, 2008, H.Hrg. 110-76 (Washington: GPO, 2008), p. 2.

³ U.S. Small Business Administration, “SBA Lending Statistics for Major Programs (as of 9/30/2011),” Washington, DC, <http://www.sba.gov/sites/default/files/hppscan41.pdf>. The SBA no longer publishes the number and amount of 7(a) loans disbursed. Based on previous experience, the number of loans approved annually ranges from about 7% to 10% higher than the number of loans disbursed (e.g., some borrowers decide not to accept the loan, there is a change in business ownership, etc.).

⁴ U.S. Small Business Administration, “Express and Pilot Programs,” Washington, DC, <http://www.sba.gov/content/express-programs>. The SBA also administers four special purpose loan guaranty programs that address particular business needs: the Community Adjustment and Investment Program (CAIP), CAPLines Program, Employee Trusts Program, and Pollution Control Program (currently not funded). See U.S. Small Business Administration, “Special Purpose Loans Program,” Washington, DC, <http://www.sba.gov/category/navigation-structure/loans-grants/small-business-loans/sba-loan-programs/7a-loan-program/special-purpose-loans-program>.

⁵ U.S. Government Accountability Office, *Small Business Administration: 7(a) Loan Program Needs Additional Performance Measures*, GAO-08-226T, November 1, 2007, pp. 3, 9-11, <http://www.gao.gov/new.items/d08226t.pdf>; and Veronique de Rugy, *Why the Small Business Administration’s Loan Programs Should Be Abolished*, American Enterprise Institute for Public Policy Research, AEI Working Paper #126, April 13, 2006, http://www.aei.org/docLib/20060414_wp126.pdf. Proponents of federal funding for the SBA’s loan guarantee programs also argue that small business can promote competitive markets. See, P.L. 83-163, §2(a), as amended; and 15 U.S.C. §631a.

⁶ Federal Reserve Board, “Senior Loan Officer Opinion Survey on Bank Lending Practices,” Washington, DC, <http://www.federalreserve.gov/boarddocs/SnLoanSurvey/>.

This report examines the 7(a) program's borrower and lender eligibility standards and program requirements, and its statistics, including loan volume, loss rates, use of the proceeds, borrower satisfaction, and borrower demographics.

It also examines congressional action taken during the 111th Congress to revise the program in an effort to help small businesses gain greater access to capital. For example, in 2009, Congress approved P.L. 111-5, the American Recovery and Reinvestment Act of 2009 (ARRA). It provided an additional \$730 million for SBA programs, including \$375 million to temporarily reduce fees in the 7(a) and 504/CDC loan guaranty programs and increase the 7(a) program's maximum guaranty percentage from up to 85% of loans of \$150,000 or less and up to 75% of loans exceeding \$150,000 to 90% for all standard 7(a) loans. Congress subsequently appropriated an additional \$265 million, and authorized the SBA to reprogram another \$40 million, to extend the fee reductions and the 7(a) program's 90% maximum loan guaranty percentage through May 31, 2010.⁷

In 2010, P.L. 111-240, the Small Business Jobs Act of 2010, increased the 7(a) program's loan guaranty limit from \$2 million to \$5 million and provided \$510 million to extend the 7(a) program's maximum loan guaranty percentage to 90% and continue the fee subsidies for the 7(a) and 504/CDC loan guaranty programs through December 31, 2010.⁸ The act also directed the SBA to establish an alternative size standard for the 7(a) and 504/CDC loan programs. This provision was designed to increase the number of small businesses that are eligible to participate in these programs. Also, P.L. 111-322, the Continuing Appropriations and Surface Transportation Extensions Act, 2011, authorized the SBA to use any funds remaining from the Small Business Jobs Act of 2010 to continue the fee subsidies and the 7(a) program's 90% maximum loan guaranty percentage through March 4, 2011, or until the available funding was exhausted. The funds were exhausted on January 3, 2011.⁹

This report also examines issues raised concerning the SBA's administration of the 7(a) program, including the oversight of 7(a) lenders and the program's lack of outcome-based performance measures. It also provides information concerning the 7(a) program's SBAExpress, Patriot Express, Small Loan Advantage, and Community Advantage programs.

⁷ P.L. 111-118, the Department of Defense Appropriations Act, 2010, provided the SBA \$125 million to continue the fee subsidies and 90% maximum loan guaranty percentage through February 28, 2010. P.L. 111-144, the Temporary Extension Act of 2010, provided the SBA \$60 million to continue the fee subsidies and 90% maximum loan guaranty percentage through March 28, 2010. P.L. 111-150, an act to extend the Small Business Loan Guarantee Program, and for other purposes, provided the SBA authority to reprogram \$40 million in previously appropriated funds to continue the fee subsidies and 90% maximum loan guaranty percentage through April 30, 2010. P.L. 111-157, the Continuing Extension Act of 2010, provided the SBA \$80 million to continue the SBA's fee subsidies and 90% maximum loan guaranty percentage through May 31, 2010.

⁸ P.L. 111-240, the Small Business Jobs Act of 2010, provided \$505 million to extend the 7(a) program's temporary increase in its maximum loan guaranty percentage and fee subsidies for the 7(a) and 504/CDC loan guaranty programs and \$5 million for related administrative expenses.

⁹ On January 3, 2011, the SBA announced that it had formed a SBA Loan Queue for loan applicants should any funding with the enhancements should become available from loan cancellations. Typically, 7% to 10% of previously approved SBA loans are later cancelled by the borrower or lender and are not disbursed for a variety of reasons. See U.S. Small Business Administration, "Jobs Act Supported More Than \$12 Billion in SBA Lending to Small Businesses in Just Three Months," Washington, DC, January 3, 2011, <http://www.sba.gov/content/jobs-act-supported-more-12-billion-sba-lending-small-businesses-just-three-months>.

Borrower Eligibility Standards and Program Requirements

Borrower Eligibility Standards

To be eligible for an SBA business loan, a small business applicant must

- be located in the United States;
- be a for-profit operating business (except for loans to eligible passive companies);
- qualify as small under the SBA's size requirements;¹⁰
- demonstrate a need for the desired credit; and
- be certified by a lender that the desired credit is unavailable to the applicant on reasonable terms and conditions from non-Federal sources without SBA assistance.¹¹

To qualify for an SBA 7(a) loan, applicants must be creditworthy and able to reasonably assure repayment. SBA requires lenders to consider the applicant's

- character, reputation, and credit history;
- experience and depth of management;
- strength of the business;
- past earnings, projected cash flow, and future prospects;
- ability to repay the loan with earnings from the business;
- sufficient invested equity to operate on a sound financial basis;
- potential for long-term success;
- nature and value of collateral (although inadequate collateral will not be the sole reason for denial of a loan request); and
- affiliates' effect on the applicant's repayment ability.¹²

¹⁰ For further analysis, see CRS Report R40860, *Defining Small Business: A Historical Analysis of Contemporary Issues*, by Robert Jay Dilger.

¹¹ 13 C.F.R. §120.100; and 13 C.F.R. §120.101. A list of ineligible businesses, such as non-profit businesses, insurance companies, and businesses deriving more than one-third of gross annual revenue from legal gambling activities, are contained in 13 C.F.R. §120.110.

¹² 13 C.F.R. §120.150.

Borrower Program Requirements

Use of Proceeds

Borrowers may use 7(a) loan proceeds to establish a new business or to assist in the operation, acquisition, or expansion of an existing business. 7(a) loan proceeds may be used to

- acquire land (by purchase or lease);
- improve a site (e.g., grading, streets, parking lots, landscaping), including up to 5% for community improvements such as curbs and sidewalks;
- purchase one or more existing buildings;
- convert, expand, or renovate one or more existing buildings;
- construct one or more new buildings;
- acquire (by purchase or lease) and install fixed assets;
- purchase inventory, supplies, and raw materials;
- finance working capital; and
- refinance certain outstanding debts.¹³

Borrowers are prohibited from using 7(a) loan proceeds to

- refinance existing debt where the lender is in a position to sustain a loss and the SBA would take over that loss through refinancing;
- effect a partial change of business ownership or a change that will not benefit the business;
- permit the reimbursement of funds owed to any owner, including any equity injection or injection of capital for the business's continuance until the loan supported by the SBA is disbursed;
- repay delinquent state or federal withholding taxes or other funds that should be held in trust or escrow; or
- pay for a non-sound business purpose.¹⁴

Loan Amounts

As mentioned previously, P.L. 111-240 increased the 7(a) program's maximum loan amount for any one 7(a) loan from \$2 million to \$5 million. The act also provided \$510 million to extend the program's temporary 90% maximum loan guaranty percentage for all standard 7(a) loans and the temporary fee reductions for the 7(a) and 504/CDC programs through December 31, 2010 (later

¹³ 13 C.F.R. §120.120.

¹⁴ 13 C.F.R. §120.130; and U.S. Small Business Administration, "Use of 7(a) Loan Proceeds," Washington, DC, <http://www.sba.gov/content/use-7a-loan-proceeds>.

extended to March 4, 2011), or until the available funding was exhausted.¹⁵ The available funding was exhausted on January 3, 2011.¹⁶

Loan Terms, Interest Rate, and Collateral

Loan Terms

7(a) loans are required to have the shortest appropriate term, depending upon the borrower's ability to repay. The maximum term is 10 years, unless the loan finances or refinances real estate or equipment with a useful life exceeding 10 years. In that case, the loan term can be up to 25 years, including extensions.¹⁷

Interest Rate

Lenders are allowed to charge borrowers "a reasonable fixed interest rate" or, with the SBA's approval, a variable interest rate.¹⁸ The SBA uses a multi-step formula to determine the maximum allowable fixed interest rate and periodically publishes that rate and the maximum allowable variable interest rate in the *Federal Register*.¹⁹

The maximum allowable fixed interest rates in November 2011 for 7(a) loans with maturities less than seven years are 7.20% for loans greater than \$50,000, 8.20% for loans over \$25,000 but not exceeding \$50,000, and 9.20% for loans of \$25,000 or less. The maximum allowable fixed interest rates in November 2011 for 7(a) loans with maturities of seven years or more are 7.70% for loans greater than \$50,000, 8.70% for loans over \$25,000 but not exceeding \$50,000, and 9.70% for loans of \$25,000 or less.²⁰

¹⁵ P.L. 111-240, the Small Business Jobs Act of 2010, provided \$505 million to extend the 7(a) program's temporary increase in its maximum loan guaranty percentage and the fee subsidies and \$5 million for related administrative expenses. P.L. 111-322, the Continuing Appropriations and Surface Transportation Extensions Act, 2011, authorizes the SBA to use funds remaining from the Small Business Jobs Act of 2010 to continue the fee subsidies and the 7(a) program's 90% maximum loan guaranty percentage through March 4, 2011, or until the available funding was exhausted.

¹⁶ U.S. Small Business Administration, "Jobs Act Supported More Than \$12 Billion in SBA Lending to Small Businesses in Just Three Months," Washington, DC, January 3, 2011, <http://www.sba.gov/content/jobs-act-supported-more-12-billion-sba-lending-small-businesses-just-three-months>.

¹⁷ 13 C.F.R. §120.212. A portion of a 7(a) loan used to acquire or improve real property may have a term of 25 years plus an additional period needed to complete the construction or improvements.

¹⁸ 13 C.F.R. §120.213.

¹⁹ For fixed interest rates, the SBA first calculates a fixed base rate using the 30 day London Interbank Offered Rate (LIBOR) in effect on the first business day of the month as published in a national financial newspaper published each business day, adds to that 300 basis points (3%) and the average of the 5-year and 10-year LIBOR swap rates in effect on the first business day of the month as published in a national financial newspaper published each business day. For 7(a) fixed loans with maturities of less than seven years, the SBA adds 2.25% to the fixed base rate to arrive at the maximum allowable fixed rate. For 7(a) fixed loans with maturities of seven years or longer, the SBA adds 2.75% to the fixed base rate to arrive at the maximum allowable fixed rate. Lenders may increase the maximum fixed interest rate allowed by an additional 1% if the fixed rate loan is over \$25,000 but not exceeding \$50,000, and by an additional 2% if the fixed rate loan is \$25,000 or less. See, U.S. Small Business Administration, "Business Loan Program Maximum Allowable Fixed Rate," 74 *Federal Register* 50263, 50264, September 30, 2009.

²⁰ Colson Services Corp., "SBA Base Rates," New York, <http://www.colsonservices.com/main/news.shtml>.

The 7(a) program's maximum allowable variable interest rate may be pegged to the lowest prime rate (3.25% in November 2011), the 30 day LIBOR rate plus 300 basis points (3.25% in November 2011), or the SBA optional peg rate (3.13% in the first quarter of FY2012).²¹ The optional peg rate is a weighted average of rates the federal government pays for loans with maturities similar to the average SBA loan.²²

Collateral

The SBA requires lenders to collateralize the loan to the maximum extent possible up to the loan amount. If business assets do not fully secure the loan, the lender must take available personal assets of the principals as collateral. Loans are considered "fully secured" if the lender has taken security interests in all available assets with a combined "liquidation value" up to the loan amount.²³

Lender Eligibility Standards and Program Requirements

Lender Eligibility Standards

Lenders must have a continuing ability to evaluate, process, close, disburse, service, and liquidate small business loans; be open to the public for the making of such loans (and not be a financing subsidiary, engaged primarily in financing the operations of an affiliate); have continuing good character and reputation; and be supervised and examined by a state or federal regulatory authority, satisfactory to SBA. They must also maintain satisfactory performance, as determined by SBA through on-site review/examination assessments, historical performance measures (such as default rate, purchase rate, and loss rate), and loan volume to the extent that it affects performance measures.²⁴

Lender Program Requirements

The Application Process

Borrowers submit applications for a 7(a) business loan to private lenders. The lender reviews the application and decides if it merits a loan on its own or if it has some weaknesses which, in the lender's opinion, do not meet standard, conventional underwriting guidelines and requires additional support in the form of an SBA guaranty. The SBA guaranty assures the lender that if the borrower does not repay the loan and the lender has adhered to all applicable regulations

²¹ Ibid.

²² U.S. Small Business Administration, "7(a) Loan Program: Terms and Conditions," Washington, DC, <http://www.sba.gov/content/7a-terms-conditions>.

²³ U.S. Small Business Administration, "SOP 50 10 5(D): Lender and Development Company Loan Programs," Washington, DC (effective October 1, 2011), p. 185, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

²⁴ 13 C.F.R. §120.410.

concerning the loan, the SBA will reimburse the lender for its loss, up to the percentage of the SBA's guaranty. The small business borrowing the money remains obligated for the full amount due.²⁵

If the lender determines that it is willing to provide the loan, but only with an SBA guaranty, it submits the application for approval through the mail, website, or e-mail to the Standard 7(a) Loan Guaranty Processing Center operating out of two locations: Citrus Heights, CA, and Hazard, KY.²⁶ This center has responsibility for processing 7(a) loan guaranty applications for lenders who do not have delegated authority to make 7(a) loans without the SBA's final approval.²⁷ The application must include the following documentation and forms:

- SBA Form 4, Application for Loan, which includes specific requirements for providing financial assistance to a small business located in a floodplain or a wetland, the use of lead-based paint, seismic safety of federal and federally assisted or regulated new building construction, coastal barrier protections, laws prohibiting discrimination on the grounds of race, color, national origin, religion, sex, marital status, disability or age, and rights under the Financial Privacy Act of 1978 (P.L. 95-630);
- SBA Form 4, Schedule A—Schedule of Collateral, or the lender may use their own form to list collateral and label it “Exhibit A”;
- SBA Form 912, Statement of Personal History—required of all principals, officers, directors and owners of 20% or more of the small business applicant;
- 7(a) Eligibility Questionnaire;
- Personal Financial Statement, dated within 90 days of submission to the SBA, on all owners of 20% or more (including the assets of the owner's spouse and any minor children), and proposed guarantors. SBA Form 413 is available. However, lenders may use their own form;
- Business Financial Statements dated within 90 days of submission to the SBA, consisting of (1) year end balance sheets for the last three years, (2) year end profit and loss statements for the last three years, (3) reconciliation of net worth, (4) interim balance sheet, (5) interim profit and loss statements, (6) affiliate and subsidiary financial statement requirements, and (7) cash flow projection—month-by-month for one year if less than three fiscal years provided and for all loans with a term of 18 months or less;
- history of the business, résumés of principals, and copy of lease, if applicable;
- detailed listing of machinery and equipment to be purchased with loan proceeds and cost quotes;

²⁵ U.S. Small Business Administration, “7(a) Loan Program: How the Program Works,” Washington, DC, http://archive.sba.gov/financialassistance/borrowers/guaranteed/7alp/FINANCIAL_GLP_7A_WORK.html.

²⁶ U.S. Small Business Administration, “SOP 50 10 5(D): Lender and Development Company Loan Programs,” Washington, DC (effective October 1, 2011), p. 221, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

²⁷ U.S. Government Accountability Office, *Small Business Administration: Opportunities Exist to Build on Leadership's Efforts to Improve Agency Performance and Employee Morale*, GAO-08-995, September 24, 2008, p. 3, <http://www.gao.gov/new.items/d08995.pdf>.

- if real estate is to be purchased with loan proceeds an appraisal, lender's environmental questionnaire, cost breakdown, and copy of purchase agreement;
- if purchasing an existing business with loan proceeds a (1) copy of buy-sell agreement, (2) pro forma balance sheet for the business being purchased as of the date of transfer, (3) copy of seller's financial statements for the last three complete fiscal years or for the number of years in business if less than three years; (4) interim statements no older than 90 days from date of submission to SBA, and (5) if seller's financial statements are not available the seller must provide an alternate source of verifying revenues;
- Equity Injection Form—explanation of type and source of applicant's equity injection;
- Franchise Form—if listed on www.franchiseregistry.com a certification of material change or certification of no change or non-material change is required. If not listed on the registry, a copy of the Franchise Agreement and Federal Trade Commission Disclosure Report of Franchisor must be submitted;
- SBA Form 159 (7a), Fee Disclosure and Compensation Agreement, must be completed for each agent compensated by the applicant or lender and retained in lender's loan file;
- a copy of Internal Revenue Service (IRS) Form 4506-T, Request for Copy of Tax Return—lender must identify the date IRS Form 4506-T was sent to IRS;
- for non-citizens, a copy of the U.S. Citizenship and Immigration Services (USCIS) Form G-845, Document Verification Request—prior to disbursement, lenders must verify the USCIS status of each alien who is required to submit USCIS documents to determine eligibility. The lender must document the findings in the loan file;
- SBA Form 4-I, Lender's Application for Guaranty—must be completed in its entirety, including pro forma balance sheet and submitted with (1) explanation of use of proceeds and benefits of the loan, (2) lender's internal credit memorandum, (3) justification for new business, including change of ownership. For new businesses and change of ownership where historical repayment ability is not demonstrated, lender must provide a narrative addressing the business plan and cite any areas of concern and justification to overcome them, and (4) business valuation must be supplied by lender for change of ownerships;
- SBA Form 1846, Statement Regarding Lobbying, must be signed and dated by lender; and
- SBA National 7(a) Authorization Boilerplate language on-line “wizard” must be completed.²⁸

A lender participating in the SBA's Certified Lenders Program (CLP), which is designed to provide expeditious service on loan applications received from lenders who have a successful SBA lending track record and a thorough understanding of SBA policies and procedures, must

²⁸ U.S. Small Business Administration, “SOP 50 10 5(D): Lender and Development Company Loan Programs,” Washington, DC (effective October 1, 2011), pp. 212-215, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

submit all forms and exhibits listed above for the standard 7(a) application. CLP lenders also must submit a draft Authorization. For loan applications greater than \$350,000, in addition to all of the standard 7(a) forms and exhibits, the lender must submit a copy of its written credit analysis and must discuss SBA eligibility issues.²⁹

A lender participating in the SBA's Preferred Lenders Program (PLP), which is designed to streamline the procedures necessary to provide financial assistance to small businesses by delegating the final credit decision and most servicing and liquidation authority and responsibility to carefully selected PLP lenders, must complete and retain in the lender's file all forms and exhibits listed above for the Standard 7(a) application.³⁰ They must submit the following forms to the SBA for review: (1) a copy of page 1 of SBA Form 4, Application for Business Loan, (2) a copy of page 1 of SBA Form 4-I, Lender's Application for Guaranty or Participation (signed by two authorized officials of the lender), (3) a copy of Form 1920SX (Part B) "Supplemental Information for PLP/SBA Express Processing," and (4) a copy of Form 7, "Eligibility Information for Preferred Lender Participation (PLP) Loans." If the PLP loan is to refinance debt (not same institution debt), a fully completed business indebtedness schedule must be attached. If the PLP loan is to finance change of ownership and a business valuation is performed by the lender, a synopsis of the analysis must be submitted.³¹

SBA Guaranty and Servicing Fees

To offset its costs, the SBA charges lenders a guaranty fee and a servicing fee for each loan approved and disbursed. The maximum guaranty fee for 7(a) loans with maturities exceeding 12 months is set by statute. Also, the servicing fee cannot exceed 0.55% per year of the outstanding balance of the SBA's share of the loan. Since 2005, the SBA has recommended that these fees be set at levels consistent with the goal of achieving a zero subsidy rate, meaning that the loan guaranty program does not require annual appropriations of budget authority for new loan guaranties.³² However, in recent years, the fees have not generated enough revenue to cover loan

²⁹ Ibid., pp. 216, 217. CLP lenders are expected to perform a complete analysis of the application and, in return, the SBA promises a faster loan decision. The SBA still makes the final credit and eligibility decision, but by completing a credit review instead of an independently conducted analysis, the SBA attempts to arrive at its decision in three working days. See, U.S. Small Business Administration, "The Certified Lenders Program (CLP)," Washington, DC, <http://www.sba.gov/content/steps-participating-clp>.

³⁰ There were 545 lenders participating in the Preferred Lenders Program in FY2011. They approved 15,167 7(a) program loans in FY2011, amounting to \$10.6 billion. The number of lenders participating in the Certified Lenders Program was not available. U.S. Small Business Administration, Office of Congressional and Legislative Affairs, "Correspondence with the author," Washington, DC, October 12, 2011.

³¹ U.S. Small Business Administration, "SOP 50 10 5(D): Lender and Development Company Loan Programs," Washington, DC (effective October 1, 2011), p. 217, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf). Lenders are considered for PLP status based on their record with SBA, and must have demonstrated a proficiency in processing and servicing SBA-guaranteed loans. The SBA continues to review the submitted materials to check loan eligibility criteria. See, U.S. Small Business Administration, "The Preferred Lenders Program (PLP)," Washington, DC, <http://www.sba.gov/content/preferred-lenders-program-plp>.

³² U.S. Congress, Senate Committee on Homeland Security and Governmental Affairs, Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security, *Small Business Administration: Is the 7(a) Program Achieving Measurable Outcomes?*, 110th Cong., 1st sess., November 1, 2007, S.Hrg. 110-605 (Washington: GPO, 2008), p. 13; and U.S. Government Accountability Office, *Small Business Administration: Additional Guidance on Documenting Credit Elsewhere Decisions Could Improve 7(a) Program Oversight*, GAO-09-228, February 12, 2009, p. 8, <http://www.gao.gov/new.items/d09228.pdf>.

losses, resulting in the need for additional appropriations to account for the shortfall—estimated to exceed \$200 million in FY2012 for the 7(a) and 504/CDC loan guaranty programs.³³

The 7(a) program's guaranty fee is based on loan maturity and the amount of the guaranty portion of the loan. For loans with a maturity of 12 months or less, the SBA charges the lender a 0.25% guaranty fee, which the lender is required to submit with the application. The lender may charge the borrower for the fee when the loan is approved by the SBA.³⁴

For loans with a maturity exceeding 12 months, the SBA charges the lender a 2% guaranty fee for the SBA guaranteed portion of loans of \$150,000 or less, a 3% guaranty fee for the SBA guaranteed portion of loans exceeding \$150,000 but not more than \$700,000, and a 3.5% guaranty fee for the SBA guaranteed portion of loans exceeding \$700,000. Loans with an SBA guaranteed portion in excess of \$1 million are charged an additional 0.25% guaranty fee on the guaranteed amount in excess of \$1 million.³⁵ These fees are the maximum allowed by law.³⁶ The lender must pay the SBA guaranty fee within 90 days of the date of loan's approval and may charge the borrower for the fee after the lender has made the first disbursement of the loan. Lenders are permitted to retain 25% of the up-front guaranty fee on loans with a gross amount of \$150,000 or less.³⁷

The annual ongoing servicing fee for all 7(a) loans is required to be no more than the "rate necessary to reduce to zero the cost to the Administration" of making guaranties and, as mentioned previously, cannot exceed 0.55% of the outstanding balance of the guaranteed portion of the loan.³⁸ The current rate is the maximum allowed by law—0.55% of the outstanding balance of the guaranteed portion of the loan.³⁹ The lender's annual service fee to the SBA cannot be charged to the borrower.⁴⁰

In 2009 and 2010, the SBA was provided more than \$1.1 billion to subsidize fees for the 7(a) and 504/CDC loan guaranty programs and to increase the 7(a) program's maximum loan guaranty percentage to 90% for all standard 7(a) loans. The last extension was provided by P.L. 111-322,

³³ U.S. Office of Management and Budget, *The Appendix, Budget of the United States Government, Fiscal Year 2012*, Washington, DC, February 14, 2011, p. 1165, <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2012/assets/sba.pdf>; H.Rept. 112-136, Financial Services and General Government Appropriations Bill, 2012, and S.Rept. 112-79, Financial Services and General Government Appropriations Bill, 2012.

³⁴ U.S. Small Business Administration, "SOP 50 10 5(D): Lender and Development Company Loan Programs," Washington, DC (effective October 1, 2011), p. 161, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf). The fee is refundable if the loan application is withdrawn prior to SBA approval, the SBA declines to guarantee the loan, or the SBA substantially changes the loan terms and those terms are unacceptable to the lender. Also, because the SBA does not approve or decline the credit for PLP loans, PLP lenders are required to send the guaranty fee directly to the SBA Denver Finance Center within 10 business days from the date the loan number is assigned and before the lender signs the Authorization for SBA.

³⁵ 15 U.S.C. 636(a)(18)(a).

³⁶ U.S. Small Business Administration, "Small Business Jobs Act: Implementation of Conforming and Technical Amendments," 76 *Federal Register* 63544, 63545, October 13, 2011.

³⁷ U.S. Small Business Administration, "SOP 50 10 5(D): Lender and Development Company Loan Programs," Washington, DC (effective October 1, 2011), p. 161, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

³⁸ 15 U.S.C. 636(a)(23)(a).

³⁹ U.S. Small Business Administration, "SBA Information Notice: 7(a) and 504 Fees Effective On October 1, 2011," Washington, DC, September 30, 2011, <http://www.sba.gov/sites/default/files/5000-1223.pdf>.

⁴⁰ 15 U.S.C. 636(a)(23)(b).

the Continuing Appropriations and Surface Transportation Extensions Act, 2011. It authorized the SBA to use any funds remaining from the Small Business Jobs Act of 2010 to continue the fee subsidies and the 7(a) program's 90% maximum loan guaranty percentage through March 4, 2011, or until the available funding was exhausted. The available funding was exhausted on January 3, 2011.⁴¹

Lender Packaging, Servicing and Other Fees

The lender may charge an applicant "reasonable fees" customary for similar lenders in the geographic area where the loan is being made for packaging and other services. The lender must advise the applicant in writing that the applicant is not required to obtain or pay for unwanted services. These fees are subject to SBA review at any time, and the lender must refund any such fee considered unreasonable by the SBA.⁴²

The lender may also charge an applicant an additional fee if, subject to prior written SBA approval, all or part of a loan will have extraordinary servicing needs. The additional fee can not exceed 2% per year on the outstanding balance of the part requiring special servicing (e.g., field inspections for construction projects). The lender may also collect from the applicant necessary out-of-pocket expenses, including filing or recording fees, photocopying, delivery charges, collateral appraisals, environmental impact reports that are obtained in compliance with SBA policy, and other direct charges related to loan closing.⁴³ The lender is prohibited from requiring the borrower to pay any fees for goods and services, including insurance, as a condition for obtaining an SBA guaranteed loan, and from imposing on SBA loan applicants processing fees, origination fees, application fees, points, brokerage fees, bonus points, and referral or similar fees.⁴⁴

The lender is also allowed to charge the borrower a late payment fee not to exceed 5% of the regular loan payment when the borrower is more than 10 days delinquent on its regularly scheduled payment. The lender may not charge a fee for full or partial prepayment of a loan.⁴⁵

For loans with a maturity of 15 years or longer, the borrower must pay to the SBA a subsidy recoupment fee when the borrower voluntarily prepays 25% or more of its loan in any one year during the first three years after first disbursement. The fee is 5% of the prepayment amount during the first year, 3% the second year, and 1% in the third year.⁴⁶

⁴¹ P.L. 111-322, the Continuing Appropriations and Surface Transportation Extensions Act, 2011, Sec. 153; and U.S. Small Business Administration, "Jobs Act Supported More Than \$12 Billion in SBA Lending to Small Businesses in Just Three Months," Washington, DC, January 3, 2011, <http://www.sba.gov/content/jobs-act-supported-more-12-billion-sba-lending-small-businesses-just-three-months>.

⁴² 13 C.F.R. §120.221.

⁴³ Ibid.; and U.S. Small Business Administration, "SOP 50 10 5(D): Lender and Development Company Loan Programs," Washington, DC (effective October 1, 2011), p. 169, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

⁴⁴ 13 C.F.R. §120.222. A commitment fee may be charged for a loan made under the Export Working Capital Loan Program.

⁴⁵ 13 C.F.R. §120.221; and U.S. Small Business Administration, "SOP 50 10 5(D): Lender and Development Company Loan Programs," Washington, DC (effective October 1, 2011), p. 170, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

⁴⁶ 13 C.F.R. §120.223; and U.S. Small Business Administration, "SOP 50 10 5(D): Lender and Development Company Loan Programs," Washington, DC (effective October 1, 2011), p. 170, <http://www.sba.gov/sites/default/files/> (continued...)

Program Statistics

Loan Volume

As shown in **Table 1**, the total number and amount of 7(a) program loans approved by the SBA declined in FY2008 and FY2009, and then increased during FY2010 and FY2011. In FY2011, the SBA approved 53,706 7(a) loans amounting to more than \$19.6 billion.⁴⁷

The SBA attributed the increased number and amount of 7(a) loans approved in FY2010 and FY2011 largely to the 7(a) program's temporary fee subsidies and 90% maximum loan guaranty percentage, which were in place during most of FY2010 and the first quarter of FY2011.⁴⁸ **Table 1** also provides data concerning the total amount of the 7(a) program's unpaid principal balance.

Table 1. 7(a) Loan Guaranty Program, Loan Volume, FY2007-FY2011

FY	Number of Loans Approved	Amount Approved	Total Unpaid Principal Balance
2007	99,606	\$14.3 billion	\$46.1 billion
2008	69,434	\$12.7 billion	\$47.7 billion
2009	41,289	\$9.2 billion	\$48.6 billion
2010	47,002	\$12.4 billion	\$50.8 billion
2011	53,706	\$19.6 billion	\$55.2 billion

Sources: U.S. Small Business Administration, *Agency Financial Report Fiscal Year 2010*, Washington, DC, November 15, 2010, p. 7; U.S. Small Business Administration, *Fiscal Year 2011 Congressional Budget Justification and FY 2009 Annual Performance Report*, Washington, DC, pp. 36, 125; U.S. Small Business Administration, "SBA Lending Statistics for Major Programs (as of 9/30/2011)," Washington, DC, <http://www.sba.gov/sites/default/files/hppscan41.pdf>; and U.S. Small Business Administration, "Table 1 — Unpaid Principal Balance By Program," Washington, DC, http://www.sba.gov/sites/default/files/files/WDS_UPB_Report_2011Q3.pdf.

Notes: The SBA no longer publishes the number and amount of 7(a) loans disbursed. Based on previous experience, the number of loans approved annually ranges from about 7% to 10% higher than the number of

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SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf.

⁴⁷ There were \$672.8 billion in total small business bank loans (defined as loans of \$1 million or less) outstanding as of June 30, 2011. The SBA estimates that finance companies provided another \$460 billion worth of credit to small businesses in 2010, bringing the total market for small business loans to about \$1.1 trillion. The SBA's 7(a) loan guaranty program's loan amount for FY2011 (\$19.6 billion) is about 2.9% of the total amount of small business loans outstanding and about 1.8% of the total market for small business loans. The SBA's 7(a) loan guaranty program's total unpaid principal balance in FY2011 (\$55.2 billion) is about 8.2% of the total amount of small business loans outstanding and about 5.0% of the total market for small business loans. Federal Deposit Insurance Corporation, "Statistics on Depository Institutions," Washington, DC, <http://www2.fdic.gov/SDI/main.asp>; and U.S. Small Business Administration, Office of Advocacy, "Frequently Asked Questions About Small Business Finance," Washington, DC, September 2011, <http://www.sba.gov/sites/default/files/Finance%20FAQ%208-25-11%20FINAL%20for%20web.pdf>.

⁴⁸ U.S. Small Business Administration, Press Office, "Recovery Loan Incentives Spurred Continued Rebound in SBA Lending in FY2010," Washington, DC, October 4, 2010, <http://www.sba.gov/about-sba-services/7367/5527>; and U.S. Small Business Administration, "Jobs Act Supported More Than \$12 Billion in SBA Lending to Small Businesses in Just Three Months," Washington, DC, January 3, 2011, <http://www.sba.gov/content/jobs-act-supported-more-12-billion-sba-lending-small-businesses-just-three-months>.

loans disbursed (e.g., some borrowers decide not to accept the loan, there is a change in business ownership, etc.). See U.S. Small Business Administration, "SBA Lending Report for Major Programs, Fiscal Year 2010," Washington, DC, October 4, 2010, http://archive.sba.gov/idc/groups/public/documents/sba_homepage/serv_fa_lending_major_progs.pdf.

Loss Rate

Since its inception in 1953 through 2008, the SBA experienced a 5.83% loss rate (ratio of actual losses to disbursements) on its general business loans.⁴⁹ In recent years, the loss rate on the SBA's general business loans has exceeded historical averages. For example, the Obama Administration reported that "due to the economic crisis and significantly higher default claims" the SBA recorded a \$3.7 billion upward re-estimate in its subsidy costs for its loan guaranty programs in FY2010, including a \$1.5 billion net upward re-estimate for the 7(a) loan guaranty program.⁵⁰ The Administration also indicated that projected economic conditions and higher anticipated defaults "have doubled the estimated cost of new 7(a) loan guaranties in FY2012 compared with FY2010."⁵¹ The Administration also announced that it "will submit a legislative package to provide SBA the flexibility to adjust fees in the 7(a) program to enable it to be self-sustaining over time" and that "these changes in the program's fee structure would become effective for loans originated after FY 2012."⁵²

Use of Proceeds and Borrower Satisfaction

In 2008, the Urban Institute released the results of an SBA-commissioned study of the SBA's loan guaranty programs. As part of its analysis, the Urban Institute surveyed a random sample of SBA loan guaranty borrowers. The survey indicated that borrowers used 7(a) loan proceeds to

- purchase or install new equipment (34%);
- finance working capital (23%);
- acquire original business (21%);
- other (19%);
- expand or renovate current building (14%);
- purchase new building (10%);
- refinance existing debt (8%);

⁴⁹ U.S. Small Business Administration, *FY 2008 Small Business Administration (SBA) Loss Report*, Washington, DC, p. 7, http://archive.sba.gov/idc/groups/public/documents/sba_program_office/cfo_2008_loss_report.pdf. General business loans include loans in the SBA's 7(a), 8(A), FIS 8a, Economic Opportunity, Small Business Energy, Handicap Assistance, Veterans, Pollution Control, Import Export, Foreign Trade, USCAIP (NAFTA) and Reconstruction Finance Corporation Business programs.

⁵⁰ U.S. Office of Management and Budget, *The Appendix, Budget of the United States Government, Fiscal Year 2012*, Washington, DC, February 14, 2011, p. 1165, <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2012/assets/sba.pdf>; and U.S. Small Business Administration, *Summary of Performance and Financial Information, Fiscal Year 2010*, Washington, DC, February 15, 2011, http://www.sba.gov/sites/default/files/Summary%20of%20Performance_2010_0.pdf.

⁵¹ Ibid.

⁵² Ibid.

- hire additional staff (6%);
- build new building (4%);
- purchase new land (3%); and
- improve land (2%).⁵³

The Urban Institute also reported that most of the 7(a) borrowers responding to their survey rated their overall satisfaction with their 7(a) loan and loan terms as either excellent (18%) or good (50%). One out of every five 7(a) borrowers (20%) rated their overall satisfaction with their 7(a) loan and loan terms as fair, and 6% rated their overall satisfaction with their 7(a) loan and loan terms as poor (7% reported don't know or did not respond).⁵⁴ In addition, 90% of the survey's respondents reported that the 7(a) loan was either very important (62%) or somewhat important (28%) to their business success (2% reported somewhat unimportant, 3% reported very unimportant, and 4% reported don't know or did not respond).⁵⁵

Borrower Demographics

The Urban Institute found that about 9.9% of conventional small business loans are issued to minority-owned small businesses and about 16% of conventional small business loans are issued to women-owned businesses.⁵⁶ In FY2011, 21.5% of 7(a) loan recipients were minority-owned businesses (11.5% Asian, 6.5% Hispanic, 2.6% African-American, and 0.9% other minority) and 16.6% were women-owned businesses.⁵⁷ Based on its comparative analysis of conventional small business loans and the SBA's loan guaranty programs, the Urban Institute concluded:

SBA's loan programs are designed to enable private lenders to make loans to creditworthy borrowers who would otherwise not be able to qualify for a loan. As a result, there should be differences in the types of borrowers and loan terms associated with SBA-guaranteed and conventional small business loans.

Our comparative analysis shows such differences. Overall, loans under the 7(a) and 504 programs were more likely to be made to minority-owned, women-owned, and start-up businesses (firms that have historically faced capital gaps) as compared to conventional small business loans. Moreover, the average amounts for loans made under the 7(a) and 504 programs to these types of firms were substantially greater than conventional small business loans to such firms. These findings suggest that the 7(a) and 504 programs are being used by lenders in a manner that is consistent with SBA's objective of making credit available to firms that face a capital opportunity gap.⁵⁸

⁵³ Christopher Hayes, *An Assessment of Small Business Administration Loan and Investment Performance: Survey of Assisted Businesses* (Washington, DC: The Urban Institute, 2008), p. 3, http://www.urban.org/UploadedPDF/411599_assisted_business_survey.pdf. The percentage total exceeds 100 because recipients were allowed to name more than one use for the loan proceeds.

⁵⁴ *Ibid.*, p. 5.

⁵⁵ *Ibid.*

⁵⁶ Kenneth Temkin, Brett Theodos, with Kerstin Gentsch, *Competitive and Special Competitive Opportunity Gap Analysis of the 7(A) and 504 Programs* (Washington, DC: The Urban Institute, 2008), p. 13, http://www.urban.org/UploadedPDF/411596_504_gap_analysis.pdf.

⁵⁷ U.S. Small Business Administration, "SBA Lending Statistics for Major Programs (as of 9/30/2011)," Washington, DC, <http://www.sba.gov/sites/default/files/hppscan41.pdf>.

⁵⁸ Kenneth Temkin, Brett Theodos, with Kerstin Gentsch, *Competitive and Special Competitive Opportunity Gap* (continued...)

Congressional Issues

Access to Capital

Congressional interest in the 7(a) loan program has increased in recent years largely because of increased concern that small businesses might be prevented from accessing sufficient capital to enable them to assist in the economic recovery. During the 111th Congress, several laws were enacted to increase the supply and demand for capital for both large and small businesses.⁵⁹ For example, in 2008, Congress adopted P.L. 110-343, the Emergency Economic Stabilization Act of 2008, which authorized the Troubled Asset Relief Program (TARP). Under TARP, the U.S. Department of the Treasury was authorized to purchase or insure up to \$700 billion in troubled assets, including small business loans, from banks and other financial institutions. The law's intent was "to restore liquidity and stability to the financial system of the United States."⁶⁰ P.L. 111-203, the Dodd-Frank Wall Street Reform and Consumer Protection Act, reduced total TARP purchase authority from \$700 billion to \$475 billion. The Treasury Department's authority to make new financial commitments under TARP ended on October 3, 2010. The Department of the Treasury has disbursed approximately \$389 billion in TARP funds, including \$337 million to purchase SBA 7(a) loan guaranty program securities.⁶¹

Also, as mentioned previously, in 2009, ARRA provided an additional \$730 million for SBA programs, including \$375 million to temporarily reduce fees in the SBA's 7(a) and 504/CDC loan guaranty programs and increase the 7(a) program's maximum loan guaranty percentage from up to 85% of loans of \$150,000 or less and up to 75% of loans exceeding \$150,000 to 90% for all standard 7(a) loans. Congress subsequently provided another \$265 million, and authorized the SBA to reprogram another \$40 million, to extend the fee reductions and loan modification through May 31, 2010, and the Small Business Jobs Act of 2010 provided another \$510 million to extend the fee reductions and loan modification from September 27, 2010, through December 31, 2010. Also, P.L. 111-322, the Continuing Appropriations and Surface Transportation Extensions Act, 2011, authorized the use of any funding remaining from the Small Business Jobs Act of 2010 to extend the fee subsidies and 90% maximum loan guaranty percentage through March 4, 2011,

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Analysis of the 7(A) and 504 Programs (Washington, DC: The Urban Institute, 2008), p. 21, http://www.urban.org/UploadedPDF/411596_504_gap_analysis.pdf.

⁵⁹ For further analysis, see CRS Report R40985, *Small Business: Access to Capital and Job Creation*, by Robert Jay Dilger.

⁶⁰ P.L. 110-343, the Emergency Economic Stabilization Act of 2008.

⁶¹ U.S. Department of the Treasury, *Troubled Assets Relief Program Monthly 105(a) Report – November 2010*, Washington, DC, December 10, 2010, pp. 2-4, [http://www.financialstability.gov/docs/November%20105\(a\)%20FINAL.pdf](http://www.financialstability.gov/docs/November%20105(a)%20FINAL.pdf). On March 16, 2009, President Obama announced that the Department of the Treasury would use TARP funds to purchase up to \$15 billion of SBA-guaranteed loans to "immediately unfreeze the secondary market for SBA loans and increase the liquidity of community banks." The plan was deferred after it met resistance from lenders. Some lenders objected to TARP's requirement that participating lenders comply with executive compensation limits and issue warrants to the federal government. Smaller, community banks objected to the program's paperwork requirements, such as the provision of a small-business lending plan and quarterly reports. See The White House, "Remarks by the President to Small Business Owners, Community Leaders, and Members of Congress," Washington, DC, March 16, 2009, http://www.whitehouse.gov/the_press_office/Remarks-by-the-President-to-small-business-owners/.

or until the available funding was exhausted.⁶² Funding for these purposes were exhausted on January 3, 2011.

The Obama Administration argued that TARP and the additional funding for the SBA's loan guaranty programs helped to improve the small business lending environment and supported "the retention and creation of hundreds of thousands of jobs."⁶³ Critics argued that small business tax reduction, reform of financial credit market regulation, and federal fiscal restraint are the best means to assist small business economic growth and job creation.⁶⁴

Program Administration

The SBA's Office of Inspector General (OIG) and the U.S. Government Accountability Office (GAO) have independently reviewed the SBA's administration of the agency's loan guaranty programs. Both agencies have reported deficiencies in the SBA's administration of its loan guaranty programs that they argue need to be addressed, including issues involving the oversight of 7(a) lenders and the lack of outcome-based performance measures.

Oversight of 7(a) Lenders

The SBA's OIG has argued that the 7(a) loan guaranty program "is vulnerable to fraud and unnecessary losses because it relies on numerous third parties (e.g., borrowers, loan agents, and lenders)" to complete loan transactions for about 80% of the loans guaranteed annually by the SBA.⁶⁵ It has argued that the SBA needs to strengthen oversight of 7(a) lenders to "establish more robust controls to prevent waste, fraud, abuse, and inefficiencies."⁶⁶

The SBA OIG has argued that the results of its review of the 7(a) program's FY2008 lending indicate the need for strengthened lender oversight. The SBA OIG found that the SBA's estimate of improper payments for FY2008 significantly understated the level of erroneous payments in the program. The SBA reported that improper payments were 0.53% of FY2008 program outlays, whereas the SBA's OIG estimated the improper payment rate to be 29% (approximately \$248 million) of the \$869 million in loan guaranties purchased between April 1, 2007, and March 31, 2008.⁶⁷ In addition, the SBA OIG's review of a sample of 30 7(a) loans issued in FY2008 found

⁶² P.L. 111-240, the Small Business Jobs Act of 2010, Sec. 1111. Section 7(A) Business Loans. The Senate had adopted H.R. 4213, the American Workers, State, and Business Relief Act of 2010, on March 10, 2010, by a 62-36 vote. It would have provided \$560 million to extend the fee reductions and 90% loan guarantee limit through December 31, 2010. The House approved an amended version of the bill, renamed the American Jobs and Closing Tax Loopholes Act of 2010, on May 28, 2010, by a 245-171 vote. It would have provided \$505 million to extend the fee reductions and 90% loan guarantee limit through December 31, 2010. The extension provision was subsequently removed from the bill, which became P.L. 111-205, the Unemployment Compensation Extension Act of 2010.

⁶³ U.S. Small Business Administration, "Administration Announces New Small Business Commercial Real Estate and Working Capital Programs," Washington, DC, February 5, 2010, http://www.sba.gov/sites/default/files/sba_rcvry_factsheet_cre_refi.pdf.

⁶⁴ Susan Eckerly, "NFIB Responds to President's Small Business Lending Initiatives," Washington, DC, October 21, 2009, <http://www.nfib.com/newsroom/newsroom-item/cmsid/50080/>; and NFIB, "Government Spending," Washington, DC, <http://www.nfib.com/issues-elections/issues-elections-item/cmsid/49051/>.

⁶⁵ U.S. Small Business Administration, Office of Inspector General, "Semiannual Report to Congress, Fall 2009," Washington, DC, p. 5, <http://www.sba.gov/office-of-inspector-general/867/12348>.

⁶⁶ *Ibid.*, p. 3.

⁶⁷ *Ibid.*, p. 5.

that 14 of the loans lacked evidence to support lender compliance with SBA origination, servicing, or liquidation requirements, resulting in improper payments totaling \$723,293. In contrast, the SBA reported improper payments of \$4,468 on two of the sampled loans.⁶⁸

In 2009, GAO also recommended that the SBA strengthen its oversight of 7(a) program lenders. GAO argued that although the SBA's "lender risk rating system has enabled the agency to conduct some off-site monitoring of lenders, the agency does not use the system to target lenders for on-site reviews or to inform the scope of the reviews."⁶⁹ It also noted that

the SBA targets for review those lenders with the largest SBA-guaranteed loan portfolios. As a result of this approach, 97 percent of the lenders that SBA's risk rating system identified as high risk in 2008 were not reviewed. Further, GAO found that the scope of the on-site reviews that SBA performs is not informed by the lenders' risk ratings, and the reviews do not include an assessment of lenders' credit decisions.⁷⁰

GAO argued that although the SBA "has made improvements to its off-site monitoring of lenders, the agency will not be able to substantially improve its lender oversight efforts unless it improves its on-site review process."⁷¹

In a separate report concerning the SBA's administration of the 7(a) program, GAO also argued in 2009 that the SBA needs to "improve its oversight of lenders' compliance with the credit elsewhere requirement."⁷² The Small Business Act specifies that "no financial assistance shall be extended pursuant to this subsection if the applicant can obtain credit elsewhere."⁷³ The SBA provides lenders the following six reasons for certifying in its application that the borrower meets the credit elsewhere requirement:

- the business needs a longer maturity than the lender's policy permits (for example, the business needs a loan that is not on a demand basis);
- the requested loan exceeds either the lender's legal lending limit or policy limit regarding the amount that it can lend to one customer;
- the lender's liquidity depends upon selling the guaranteed portion of the loan on the secondary market;
- the collateral does not meet the lender's policy requirements;
- the lender's policy normally does not allow loans to new businesses or businesses in the applicant's industry; or

⁶⁸ Ibid.

⁶⁹ U.S. Government Accountability Office, *Small Business Administration: Actions Needed to Improve the Usefulness of the Agency's Lender Risk Rating System*, GAO-1—53, November 6, 2009, p. i, <http://www.gao.gov/new.items/d1053.pdf>.

⁷⁰ Ibid., pp. i, 27-30.

⁷¹ Ibid., p. 35.

⁷² U.S. Government Accountability Office, *Small Business Administration: Additional Guidance on Documenting Credit Elsewhere Decisions Could Improve 7(a) Program Oversight*, GAO-09-228, February 12, 2009, p. 3, <http://www.gao.gov/new.items/d09228.pdf>.

⁷³ 15 U.S.C. 636(a)(1)(A). The act defines credit elsewhere as "the availability of credit from non-Federal sources on reasonable terms and conditions taking into consideration the prevailing rates and terms in the community in or near where the concern transacts business, or the homeowner resides, for similar purposes and periods of time." See 15 U.S.C. 632(h).

- any other factors relating to the credit that, in the lender's opinion, cannot be overcome except for the guaranty. These other factors must be specifically documented in the loan file.⁷⁴

GAO argued that "SBA's guidance to lenders on documenting compliance with the credit elsewhere requirement is limited" because it "does not specify the amount of detail lenders should include in their explanations."⁷⁵ GAO noted that "even with the lack of detail required," the SBA's own on-site reviews of 7(a) lenders over a recent six-quarter period indicated that nearly a third of the lenders reviewed had not consistently documented that borrowers met the credit elsewhere requirement.⁷⁶

The SBA has argued that it currently "conducts a continuous risk-based, off-site analysis of lending partners through the Loan/Lender Monitoring System (L/LMS), a state-of-the-art portfolio monitoring system that incorporates credit scoring metrics for portfolio management purposes."⁷⁷ According to the SBA:

The Loan/Lender Monitoring System focuses on 7(a) lenders, certified development companies and microloan intermediaries that pose the most risk to the SBA. In addition to overseeing lenders, the L/LMS provides policy, portfolio and program analysis. The Office of Credit Risk Management (OCRM) is divided into four teams: large lender oversight, small lender oversight, lender transaction, and program and policy analysis. The differentiation of lender oversight by lender size reflects the different forms of oversight needed for large lenders versus small lenders.⁷⁸

The SBA asserts that

The OCRM is continually enhancing and updating oversight programs and practices to provide a more robust and responsive system. Enhancements include: (1) better integration of delegated lending decisions into oversight practices; (2) addition of different types of lender reviews (targeted, desk, agreed upon procedures, etc.) to provide more options to obtain information in the most timely and efficient manner possible; (3) assessment of current on-site review practices to customize them based on risk factors and consider credit decisions made by lenders; (4) development of a lender certification program (particularly for community lenders); (5) quarterly reporting for non-bank lenders; (6) identification/monitoring of risk related red flags and triggers; and (7) training for OCA staff, district office staff and lenders in the new process.⁷⁹

⁷⁴ U.S. Small Business Administration, "SOP 50 10 5(D): Lender and Development Company Loan Programs," Washington, DC (effective October 1, 2011), p. 102, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

⁷⁵ U.S. Government Accountability Office, *Small Business Administration: Additional Guidance on Documenting Credit Elsewhere Decisions Could Improve 7(a) Program Oversight*, GAO-09-228, February 12, 2009, pp. 25, 26, <http://www.gao.gov/new.items/d09228.pdf>.

⁷⁶ *Ibid.*, p. 26.

⁷⁷ U.S. Small Business Administration, *Fiscal Year 2011 Congressional Budget Justification and FY 2009 Annual Performance Report*, Washington, DC, p. 6.

⁷⁸ *Ibid.*, p. 43.

⁷⁹ *Ibid.*

In addition, in its FY2012 congressional budget request, the SBA reported that it had “created a more robust risk rating system, with more transparency in portfolios, and “best practices” for lender oversight (including more on-site and off-site lender monitoring).”⁸⁰

Outcome-Oriented Performance Measures

GAO has argued that the 7(a) program’s performance measures (e.g., number of loans approved, loans funded, and firms assisted across the subgroups of small businesses) provide limited information about the impact of the loans on participating small businesses:

The program’s performance measures focus on indicators that are primarily output measures—for instance, they report on the number of loans approved and funded. But none of the measures looks at how well firms do after receiving 7(a) loans, so no information is available on outcomes. As a result, the current measures do not indicate how well the agency is meeting its strategic goal of helping small businesses succeed.⁸¹

The SBA OIG has made a similar argument concerning the SBA’s Microloan program’s performance measures. Because the SBA uses similar program performance measures for its Microloan and 7(a) programs, the SBA OIG’s recommendations could also be applied to the SBA’s 7(a) program.

Specifically, as part of its audit of the SBA Microloan program’s use of ARRA funds, the SBA OIG found that the SBA’s performance measures for the Microloan program are based on the number of microloans funded, the number of small businesses assisted, and program’s loan loss rate. It argued that these “performance metrics ... do not ensure the ultimate program beneficiaries, the microloan borrowers, are truly assisted by the program” and “without appropriate metrics, SBA cannot ensure the Microloan program is meeting policy goals.”⁸² It noted that the SBA does not track the number of microloan borrowers who remain in business after receiving a microloan to measure the extent to which the loans contributed to the success of borrowers and does not determine the effect that technical training assistance may have on the success of microloan borrowers and their ability to repay loans.⁸³ It recommended that the SBA “develop additional performance metrics to measure the program’s achievement in assisting microloan borrowers in establishing and maintaining successful small businesses.”⁸⁴

In its response to GAO’s recommendation to develop additional performance measures for the 7(a) program, the SBA indicated that there are legal constraints and cost considerations associated with tracking the success or failure of SBA borrowers and that it had, at that time, “a new administrator who may make changes to the agency’s performance measures and goals.”⁸⁵ In

⁸⁰ U.S. Small Business Administration, *Fiscal Year 2012 Congressional Budget Justification and FY 2010 Annual Performance Report*, Washington, DC, p. 7.

⁸¹ U.S. Government Accountability Office, *Small Business Administration: 7(a) Loan Program Needs Additional Performance Measures*, GAO-08-226T, November 1, 2007, p. 2, <http://www.gao.gov/new.items/d08226t.pdf>.

⁸² U.S. Small Business Administration, Office of the Inspector General, *SBA’s Administration of the Microloan Program under the Recovery Act*, Washington, DC, December 28, 2009, p. 6, <http://www.sba.gov/sites/default/files/om10-10.pdf>.

⁸³ Ibid.

⁸⁴ Ibid., p. 7.

⁸⁵ U.S. Government Accountability Office, *Small Business Administration: 7(a) Loan Program Needs Additional Performance Measures*, GAO-08-226T, November 1, 2007, p. 8, <http://www.gao.gov/new.items/d08226t.pdf>.

response to the SBA OIG's recommendation to develop additional performance metrics for the Microloan program, the SBA reported that it has "contracted with the Aspen Institute to advise on appropriate program and performance metrics for both microloans and technical assistance grants."⁸⁶ It also indicated that the program metrics developed will be used to assist the agency in measuring the Microloan program's effectiveness. Given that the Microloan program and 7(a) program use similar performance measures, it could be argued that the program metrics developed for the Microloan program may be applied to the 7(a) program as well.

Legislative Activity During the 111th Congress

Congress authorized several changes to the 7(a) program during the 111th Congress in an effort to increase the number, and amount, of 7(a) loans, including provisions contained in ARRA and the Small Business Jobs Act of 2010. Congress has not approved any changes to the 7(a) program during the 112th Congress.

The Obama Administration's Proposals

During the 111th Congress, the Obama Administration supported congressional efforts to temporarily subsidize fees for the 7(a) and 504/CDC loan guaranty programs and to increase the 7(a) program's loan guaranty percentage from up to 85% of loans of \$150,000 or less and up to 75% of loans exceeding \$150,000 to 90%. As mentioned previously, Congress subsequently provided more than \$1.1 billion to subsidize fees for the 7(a) and 504/CDC loan guaranty programs and to increase the 7(a) program's maximum loan guaranty percentage to 90% for all standard 7(a) loans.

The Obama Administration also proposed the following modifications to several SBA programs, including the 7(a) program:

- increase the maximum loan size for 7(a) loans from \$2 million to \$5 million;
- increase the maximum loan size for the 504/CDC program from \$2 million to \$5 million for regular projects and from \$4 million to \$5.5 million for manufacturing projects;
- increase the maximum loan size for microloans to small business concerns from \$35,000 to \$50,000;
- increase the maximum loan limits for lenders in their first year of participation in the Microloan program, from \$750,000 to \$1 million, and from \$3.5 million to \$5 million in the subsequent years;
- temporarily increase the cap on SBAExpress loans from \$350,000 to \$1 million; and

⁸⁶ U.S. Small Business Administration, Office of the Inspector General, *SBA's Administration of the Microloan Program under the Recovery Act*, Washington, DC, December 28, 2009, p. 9, <http://www.sba.gov/sites/default/files/om10-10.pdf>.

- temporarily allow in FY2010 and FY2011, with an option to extend into FY2012, the refinancing of owner-occupied commercial real estate loans within one year of maturity under the SBA's 504/CDC program.⁸⁷

Arguments for Increasing the SBA's Maximum Loan Limits

The Obama Administration argued that increasing the maximum loan limits for the 7(a), 504/CDC, Microloan, and SBAExpress programs would allow the SBA to “support larger projects,” which will “allow the SBA to help America’s small businesses drive long-term economic growth and the creation of jobs in communities across the country.”⁸⁸ The Administration also argued that increasing the maximum loan limits for these programs will be “budget neutral” over the long run and “help improve the availability of smaller loans.”⁸⁹

Arguments Against Increasing the SBA's Maximum Loan Limits

Critics of the Obama Administration’s proposals to increase the SBA’s maximum loan limits argued that it might increase the risk of defaults, resulting in higher guaranty fees or the need to provide the SBA additional funding, especially for the SBAExpress program, which has experienced somewhat higher default rates than other SBA loan guaranty programs.⁹⁰ Others advocated a more modest increase in the maximum loan limits to ensure that the 7(a) program “remains focused on startup and early-stage small firms, businesses that have historically encountered the greatest difficulties in accessing credit” and “avoids making small borrowers carry a disproportionate share of the risk associated with larger loans.”⁹¹

Others argued that creating a small business direct lending program within the SBA would reduce paperwork requirements and be more efficient in providing small businesses access to capital than modifying existing SBA programs that rely on private lenders to determine if they will issue the loans.⁹² Also, as mentioned previously, others argued that providing additional resources to the SBA or modifying the SBA’s loan programs as a means to augment small business access to capital is ill-advised. In their view, the SBA has limited impact on small access to capital. They argued that the best means to assist small business economic growth and job creation is to focus

⁸⁷ U.S. Small Business Administration, “Administration Announces New Small Business Commercial Real Estate and Working Capital Programs,” Washington, DC, February 5, 2010, http://www.sba.gov/sites/default/files/sba_rcvry_factsheet_cre_refi.pdf.

⁸⁸ Ibid.

⁸⁹ Ibid.

⁹⁰ Robb Mandelbaum, “Small Business Incentives Face a Hard Road in Congress,” *New York Times*, February 12, 2010, <http://boss.blogs.nytimes.com/2010/02/12/small-business-incentives-face-a-hard-road-in-congress/>; and U.S. Congress, House Committee on Small Business, *House Committee on Small Business Views With Regard to the Fiscal Year (FY) 2010 Budget*, Letter from Nydia Velázquez, Chair, House Committee on Small Business, to John M. Spratt, Jr., Chair, House Committee on the Budget, 111th Cong., 2nd sess., March 11, 2009, p. 3, <http://www.house.gov/smbiz/democrats/Reports/FY%202010%20Views%20and%20Estimates%20v2.pdf>.

⁹¹ U.S. Congress, House Committee on Small Business, *Small Business Financing and Investment Act Of 2009*, report to accompany H.R. 3854, 111th Cong., 2nd sess., October 26, 2009, H.Rept. 111-315 (Washington: GPO, 2009), p. 1.

⁹² Robb Mandelbaum, “Why Won’t the S.B.A. Lend Directly to Small Businesses?” *New York Times*, March 10, 2010, <http://boss.blogs.nytimes.com/2010/03/10/why-wont-the-s-b-a-loan-directly-to-small-businesses/>.

on small business tax reduction, reform of financial credit market regulation, and federal fiscal restraint.⁹³

H.R. 3854, the Small Business Financing and Investment Act of 2009

H.R. 3854 would have authorized several new SBA programs and change several existing SBA programs, including the 7(a) program, in an effort to enhance job creation by increasing the availability of credit to small businesses. The bill was passed by the House, 389-32, on October 29, 2009. The Senate did not act on the bill.⁹⁴

It would have

- increased the maximum loan size for 7(a) loans from \$2 million to \$3 million;
- increased the maximum loan size for 504/CDC loans from \$1.5 million to \$3 million for regular projects, from \$2 million to \$4 million for projects located in a low-income community, from \$4 million to \$8 million for manufacturers, and for up to \$10 million for projects that constitute “a major source of employment” as determined by the Administration;
- extended ARRA’s fee reductions and the 7(a) program’s 90% loan guaranty limit through September 30, 2011;
- authorized the SBA to establish an alternative size standard for the 7(a) program that uses maximum tangible net worth and average net income as an alternative to the use of industry standards and established an interim size standard of a maximum tangible net worth of not more than \$15 million and an average net income after federal taxes (excluding any carryover losses) for the preceding two fiscal years of not more than \$5 million;
- extended, with modifications, ARRA’s America’s Recovery Capital Loan Program (ARC) which temporarily provides small businesses loan assistance for debt relief, through the end of FY2011;⁹⁵ and
- provided a 100% loan guaranty for small business concerns owned and controlled by veterans, and expanded and made permanent the SBA’s secondary market lending authority.⁹⁶

⁹³ Susan Eckerly, “NFIB Responds to President’s Small Business Lending Initiatives,” Washington, DC, October 21, 2009, <http://www.nfib.com/newsroom/newsroom-item/cmsid/50080/>; and NFIB, “Government Spending,” Washington, DC, <http://www.nfib.com/issues-elections/issues-elections-item/cmsid/49051/>.

⁹⁴ For further analysis, see CRS Report R40985, *Small Business: Access to Capital and Job Creation*, by Robert Jay Dilger.

⁹⁵ ARC’s loan limit would be increased from \$35,000 to \$50,000, and to \$75,000 in areas of high unemployment, and borrowers would be allowed to use ARC loans to refinance existing SBA loan debt. The ARC program ended on September 30, 2010.

⁹⁶ H.R. 3854, the Small Business Financing and Investment Act of 2009.

The bill would have also created a temporary SBA direct lending program following enactment that would be available to creditworthy small business borrowers that are unable to find credit elsewhere.⁹⁷

S. 2869, the Small Business Job Creation and Access to Capital Act of 2009

S. 2869 was ordered to be reported by the Senate Committee on Small Business and Entrepreneurship on December 10, 2009. The Senate did not take further action on the bill, but many of its provisions were later included in P.L. 111-240. It would have authorized changes to several SBA programs, including the 7(a) program, and was designed to enhance job creation by increasing the availability of credit to small businesses.

It would have

- increased the maximum loan size for 7(a) loans from \$2 million to \$5 million;
- increased the maximum loan size for the 504/CDC loans from \$1.5 million to \$5 million for regular projects, from \$2 million to \$5 million for projects meeting one of the program's specified public policy goals, and from \$4 million to \$5.5 million for manufacturers;
- increased the maximum loan size for the Microloan program from \$35,000 to \$50,000;
- extended ARRA's fee reductions and the 7(a) program's 90% loan guaranty limit through December 31, 2010;
- authorized the SBA to establish an alternative size standard for the 7(a) and 504/CDC programs that uses maximum tangible net worth and average net income as an alternative to the use of industry standards and established an interim size standard of a maximum tangible net worth of not more than \$15 million and an average net income after federal taxes (excluding any carryover losses) for the preceding two fiscal years of not more than \$5 million; and
- allowed 504/CDC loans to be used to refinance up to \$4 billion in short-term commercial real estate debt each fiscal year for two years after enactment into long-term fixed rate loans.⁹⁸

P.L. 111-240, the Small Business Jobs Act of 2010

P.L. 111-240 was signed into law by President Obama on September 27, 2010. It increased the 7(a) program's loan guaranty limit from \$2 million to \$5 million, provided \$510 million to extend the 7(a) program's 90% maximum loan guaranty percentage and 7(a) and 504/CDC loan guaranty programs' fee subsidies through December 31, 2010 (later extended to March 4, 2011), or until

⁹⁷ Ibid. For further analysis, see CRS Report R40985, *Small Business: Access to Capital and Job Creation*, by Robert Jay Dilger.

⁹⁸ S. 2869, the Small Business Job Creation and Access to Capital Act of 2009; and H.R. 4213, the American Workers, State and Business Relief Act.

available funding was exhausted (which occurred on January 3, 2011). The act also includes all of the provisions listed above in S. 2869, the Small Business Job Creation and Access to Capital Act of 2009, except that it would allow 504/CDC loans to be used to refinance up to \$7.5 billion in short-term commercial real estate debt each fiscal year for two years after enactment into long-term fixed rate loans instead of up to \$4 billion each fiscal year.⁹⁹

The act also authorizes the Secretary of the Treasury to establish a \$30 billion Small Business Lending Fund (SBLF) to encourage community banks to provide small business loans (\$4 billion was issued), a \$1.5 billion State Small Business Credit Initiative to provide funding to participating states with small business capital access programs, and about \$12 billion in tax relief for small businesses.¹⁰⁰ It also contains revenue raising provisions to offset the act's cost and authorizes a number of changes to other SBA loan and contracting programs.

Legislative Activity During the 112th Congress

As mentioned previously, Congress has not approved any changes to the 7(a) program during the 112th Congress. However, two bills have been introduced that would affect the 7(a) program's SBAExpress and Patriot Express specialized programs.

H.R. 2936, the Small Business Administration Express Loan Extension Act of 2011, introduced on September 15, 2011 and referred to the House Committee on Small Business, would extend a one-year increase in the maximum loan amount for the SBAExpress program from \$350,000 to \$1 million for an additional year. The temporary increase in that program's maximum loan amount was authorized by P.L. 111-240, the Small Business Jobs Act of 2010, and expired on September 26, 2011 (see **Appendix**).

S. 532, the Patriot Express Authorization Act of 2011, introduced on March 9, 2011 and referred to the Senate Committee on Small Business and Entrepreneurship, would provide statutory authorization for the Patriot Express Pilot Program (see **Appendix**). The bill would also increase the program's maximum loan amount from \$500,000 to \$1 million, and increase the guaranty percentage from up to 85% of loans of \$150,000 or less and up to 75% of loans exceeding \$150,000 to up to 85% of loans of \$500,000 or less and up to 80% of loans exceeding \$500,000.

Concluding Observations

The congressional debate concerning the SBA's 7(a) program during the 111th Congress was not whether the federal government should act, but which federal policies would most likely enhance small business access to capital and result in job retention and creation. As a general proposition, some, including President Obama, argued that economic conditions made it imperative that the SBA be provided additional resources to assist small businesses in acquiring capital necessary to start, continue, or expand operations with the expectation that in so doing small businesses will

⁹⁹ P.L. 111-240, the Small Business Jobs Act of 2010, Sec. 1122. Low-Interest Refinancing Under the Local Development Business Loan Program.

¹⁰⁰ For further analysis of P.L. 111-240, the Small Business Jobs Act of 2010, see CRS Report R41385, *Small Business Legislation During the 111th Congress*, by Robert Jay Dilger and Gary Guenther. For further analysis of the Small Business Lending Fund, see CRS Report R42045, *The Small Business Lending Fund*, by Robert Jay Dilger.

create jobs.¹⁰¹ Others worried about the long-term adverse economic effects of spending programs that increase the federal deficit. They advocated business tax reduction, reform of financial credit market regulation, and federal fiscal restraint as the best means to assist small business economic growth and job creation.¹⁰²

In terms of specific program changes, increasing the 7(a) program's loan limit, extending the 7(a) program's temporary fee subsidies and 90% maximum loan guaranty percentage, and establishing an alternative size standard for the 7(a) program were all designed to achieve the same goal: to enhance job creation by increasing the ability of 7(a) borrowers to access credit at affordable rates. However, determining how specific changes in federal policy are most likely to enhance job creation is a challenging question. For example, a 2008 Urban Institute study concluded that differences in the term, interest rate, and amount of SBA financing "was not significantly associated with increasing sales or employment among firms receiving SBA financing."¹⁰³ However, they also reported that their analysis accounted for less than 10% of the variation in firm performance. The Urban Institute suggested that local economic conditions, local zoning regulations, state and local tax rates, state and local business assistance programs, and the business owner's charisma or business acumen also "may play a role in determining how well a business performs after receipt of SBA financing."¹⁰⁴

As the Urban Institute study suggests, given the many factors that influence business success, measuring the SBA's 7(a) program's effect on job retention and creation is complicated. That task is made even more challenging by the absence of performance-oriented measures that could serve as a guide. Both GAO and the SBA's OIG have recommended that the SBA adopt outcome performance oriented measures for its loan guaranty programs, such as tracking the number of borrowers who remain in business after receiving a loan to measure the extent to which the program contributed to their ability to stay in business.¹⁰⁵ Other performance-oriented measures that Congress might also consider include requiring the SBA to survey 7(a) borrowers to measure the difficulty they experienced in obtaining a loan from the private sector and the extent to which the 7(a) loan or technical assistance received contributed to their ability to create jobs or expand their scope of operations.

¹⁰¹ Representative Nydia Velázquez, "Small Business Financing and Investment Act of 2009," House debate, *Congressional Record*, daily edition, vol. 155, no. 159 (October 29, 2009), pp. H12074, H12075; Senator Mary Landrieu, "Statements on Introduced Bills and Joint Resolutions," remarks in the Senate, *Congressional Record*, daily edition, vol. 155, no. 185 (December 10, 2009), p. S12910; and The White House, "Remarks by the President on Job Creation and Economic Growth," December 8, 2009, <http://www.whitehouse.gov/the-press-office/remarks-president-job-creation-and-economic-growth>.

¹⁰² Susan Eckerly, "NFIB Responds to President's Small Business Lending Initiatives," Washington, DC, October 21, 2009, <http://www.nfib.com/newsroom/newsroom-item/cmsid/50080/>; and NFIB, "Government Spending," Washington, DC, <http://www.nfib.com/issues-elections/issues-elections-item/cmsid/49051/>.

¹⁰³ Shelli B. Rossman and Brett Theodos, with Rachel Brash, Megan Gallagher, Christopher Hayes, and Kenneth Temkin, *Key Findings from the Evaluation of the Small Business Administration's Loan and Investment Programs: Executive Summary* (Washington, DC: The Urban Institute, January 2008), p. 58, http://www.urban.org/UploadedPDF/411602_executive_summary.pdf.

¹⁰⁴ Ibid.

¹⁰⁵ U.S. Government Accountability Office, *Small Business Administration: 7(a) Loan Program Needs Additional Performance Measures*, GAO-08-226T, November 1, 2007, p. 2, <http://www.gao.gov/new.items/d08226t.pdf>; and U.S. Small Business Administration, Office of the Inspector General, *SBA's Administration of the Microloan Program under the Recovery Act*, Washington, DC, December 28, 2009, pp. 6, 7, <http://www.sba.gov/sites/default/files/om10-10.pdf>.

Appendix. 7(a) Specialized Programs

The 7(a) program has four specialized programs that offer streamlined and expedited loan procedures for particular groups of borrowers, the SBAExpress, Patriot Express, Small Loan Advantage, and Community Advantage programs. Lenders must be approved by the SBA for participation in these programs.

SBAExpress Program

The SBAExpress program was established as a pilot program by the SBA on February 27, 1995, and made permanent through legislation, subject to reauthorization, in 2004 (P.L. 108-447, the Consolidated Appropriations Act, 2005). The program was designed to increase the availability of credit to small businesses by permitting lenders to use their existing documentation and procedures in return for receiving a reduced SBA guaranty on loans.¹⁰⁶ It provides a 50% loan guaranty on loan amounts up to \$350,000.

In FY2011, the SBA approved 26,836 SBAExpress loans amounting to \$2.87 billion.¹⁰⁷ In FY2010, the SBA approved 20,450 SBAExpress loans amounting to \$1.55 billion.¹⁰⁸ The higher loan volume for the program in FY2011 was due, at least in part, to P.L. 111-240, the Small Business Jobs Act of 2010, which temporarily increased the SBAExpress program's loan limit to \$1 million for one year following enactment (through September 26, 2011).¹⁰⁹

SBAExpress loan proceeds can be used for the same purposes as the 7(a) program (expansion, renovation, new construction, the purchase of land or buildings, the purchase of equipment, fixtures, and lease-hold improvements, working capital, to refinance debt for compelling reasons, seasonal line of credit, and inventory) except participant debt restructure cannot exceed 50% of the project and may be used for revolving credit. The program's loan terms are the same as the 7(a) program (the loan maturity for working capital, machinery, and equipment (not to exceed the life of the equipment) is typically 5 to 10 years and the loan maturity for real estate is up to 25 years), except that the term for a revolving line of credit cannot exceed 7 years.

The SBAExpress loan's interest rates are negotiable with the lender, subject to maximums. Rates can be fixed or variable. Fixed rates may not exceed prime plus 6.5% on loans of \$50,000 or less and prime plus 4.5% on loans over \$50,000. Variable interest rates are based on either the prime rate (as published in *The Wall Street Journal*), the 30-day LIBOR plus 3.0%, or the SBA's optional peg rate (published quarterly in the *Federal Register*) plus 6.5% on loans of \$50,000 or less and plus 4.5% on loans over \$50,000.¹¹⁰ The program's fees are the same as the 7(a) program. To account for the program's lower guaranty rate of 50%, lenders are allowed to

¹⁰⁶ U.S. Small Business Administration, "The SBA Express Pilot Program: Inspection Report," Washington, DC, June 1998, p. 3, http://archive.sba.gov/idc/groups/public/documents/sba/oig_loarchive_980601.pdf.

¹⁰⁷ U.S. Small Business Administration, "SBA Lending Statistics for Major Programs (as of 9/30/2011)," Washington, DC, <http://www.sba.gov/sites/default/files/hppscan41.pdf>.

¹⁰⁸ Ibid.

¹⁰⁹ H.R. 2936, the Small Business Administration Express Loan Extension Act of 2011, would extend the higher loan limit for an additional year.

¹¹⁰ U.S. Small Business Administration, "SBAExpress," Washington, DC, http://archive.sba.gov/financialassistance/prospectivelenders/7a/ep/FA_PL_7ALOAN_SBAEXPRESS.html.

perform their own loan analysis and procedures and receive SBA approval with a targeted 36-hour maximum turnaround time.¹¹¹ Also, collateral is not required for loans of \$25,000 or less. Lenders are allowed to use their own established collateral policy for loans over \$25,000.

Patriot Express Pilot Program

In 2007, the SBA created the Patriot Express Pilot Program “to support the entrepreneur segment of the Nation’s military community (including spouses).”¹¹² Eligible businesses must be owned and controlled (51% or more) by one or more of the following groups: veteran, active duty military participating in the military’s Transition Assistance Program, reservist or national guard member or a spouse of any of these groups, a widowed spouse of a service member who died while in service, or a widowed spouse of a veteran who died of a service-connected disability.¹¹³ The SBA announced on December 10, 2010, that it will continue to operate the program for at least three more years.¹¹⁴

The Patriot Express Pilot Program provides the same loan guaranty as the 7(a) program on loan amounts up to \$500,000 (up to 85% of loans of \$150,000 or less and up to 75% of loans exceeding \$150,000). The loan proceeds can be used for the same purposes as the 7(a) program (expansion, renovation, new construction, the purchase of land or buildings, the purchase of equipment, fixtures, and lease-hold improvements, working capital, to refinance debt for compelling reasons, seasonal line of credit, and inventory) except participant debt restructure cannot exceed 15-25% of the project and may be used for revolving lines of credit. The loan terms are the same as the 7(a) program (the loan maturity for working capital, machinery, and equipment (not to exceed the life of the equipment) is typically 5 to 10 years and the loan maturity for real estate is up to 25 years), except that the term for a revolving line of credit cannot exceed 7 years. Also, collateral is not required for loans of \$25,000 or less. Lenders are allowed to use their own established collateral policy for loans over \$25,000 and up to \$350,000. For loans exceeding \$350,000, lenders must follow the SBA’s regulations on collateral for standard 7(a) loans.¹¹⁵

The Patriot Express Pilot Program features streamlined documentation and processing features similar to the SBAExpress program, with a targeted SBA processing time of one business day. The program’s interest rates are negotiable with the lender, subject to the same maximum rate limitations as the 7(a) program. It also has the same fees as the 7(a) program.¹¹⁶

¹¹¹ Ibid.

¹¹² U.S. Small Business Administration, “SOP 50 10 5(D): Lender and Development Company Loan Programs,” Washington, DC (effective October 1, 2011), p. 42, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

¹¹³ Ibid., pp. 83, 127.

¹¹⁴ U.S. Small Business Administration, “Popular SBA Patriot Express Loan Initiative Renewed for Three More Years,” Washington, DC, December 10, 2010, <http://www.sba.gov/content/popular-sba-patriot-express-loan-initiative-renewed-three-more-years>. S. 532, the Patriot Express Authorization Act of 2011, would provide the program statutory authorization.

¹¹⁵ U.S. Small Business Administration, “SOP 50 10 5(D): Lender and Development Company Loan Programs,” Washington, DC (effective October 1, 2011), p. 83, 147, 150-152, [http://www.sba.gov/sites/default/files/SOP%2050%2010%205\(D\)%20\(9-15-11\)%20clean_0.pdf](http://www.sba.gov/sites/default/files/SOP%2050%2010%205(D)%20(9-15-11)%20clean_0.pdf).

¹¹⁶ Ibid., pp. 86, 178.

The SBA has indicated in both testimony at congressional hearings and in press releases that it views the Patriot Express Program as a success. For example, in 2007, William Elmore, Associate Director of the SBA's Office of Veterans Business Development, testified at a congressional hearing shortly after the Patriot Express program's rollout that

so far, the results have been good. The number of loans made to veterans increased from 4,800 in fiscal year 2000 to approximately 8,000 loans in fiscal year 2006.¹¹⁷

In 2010, Joseph Jordan, SBA's Associate Administrator for Contracting and Business Development, testified at a congressional hearing that

SBA is committed to assisting veteran-owned small businesses access the capital they need. All of SBA's loan programs are available to veterans. In FY2009, veteran-owned small businesses received 8.00% of all 7(a) loans, totaling approximately \$523 million, and 4.56% of all 504 development company loans, or \$176 million. Additionally, veteran-owned small businesses received 4.33% of all microloans, totaling approximately \$1.9 million. In total, SBA has supported more than \$2 billion in recovery lending to veteran-owned small businesses. SBA also has a loan program dedicated to the military community—Patriot Express.... It features our lowest interest rates and fastest turnaround times, often within days.... In FY2009, we approved more than 2,300 Patriot Express loans and are on track to increase those numbers in FY2010.¹¹⁸

More recently, when the SBA announced in a December 10, 2010, press release that it was extending the Patriot Express Loan Program for another three years, the SBA characterized the program as "a very popular initiative that in just three-and-a-half years has provided more than \$560 million in loan guarantees to nearly 7,000 veterans to start or expand their small businesses."¹¹⁹

Congressional testimony provided by various veteran service organizations provides a different perspective. For example, a representative of the American Legion testified at a congressional hearing in 2010 that being turned down for a SBA Patriot Express loan "is probably the largest, most frequent complaint that we receive from our business owners."¹²⁰ At that same congressional hearing, a representative of the Vietnam Veterans of America testified in response to that statement that

I would have to concur ... in talking with some of the veterans with regard to the Patriot Express Loan, they are having difficulties also to acquire that capital. The rationale seems to

¹¹⁷ U.S. Congress, Senate Committee on Small Business and Entrepreneurship, *Assessing Federal Small Business Assistance Programs for Veterans and Reservists*, hearing, 110th Cong., 1st sess., January 31, 2007, S.Hrg. 110-209 (Washington: GPO, 2007), p. 32.

¹¹⁸ U.S. Congress, House Committee on Veterans' Affairs, Subcommittee on Economic Opportunity, *Status of Veterans Small Business*, hearing, 111th Cong., 2nd sess., April 29, 2010, House Committee on Veterans' Affairs Serial No. 111-74 (Washington: GPO, 2010), p. 75.

¹¹⁹ U.S. Small Business Administration, "Popular SBA Patriot Express Loan Initiative Renewed for Three More Years," Washington, DC, December 10, 2010, <http://www.sba.gov/content/popular-sba-patriot-express-loan-initiative-renewed-three-more-years>.

¹²⁰ U.S. Congress, House Committee on Veterans' Affairs, Subcommittee on Economic Opportunity, *Status of Veterans Small Business*, hearing, 111th Cong., 2nd sess., April 29, 2010, House Committee on Veterans' Affairs Serial No. 111-74 (Washington: GPO, 2010), p. 17.

be ... the banks in general seem to be tightening the credit, their lending practices, so that is ... what we are hearing.¹²¹

There are no empirical assessments of veterans' experiences with the SBA Patriot Express Loan program that would be useful for determining the relative ease or difficulty of veteran-owned small business owners accessing capital through the program.¹²² The SBA does not conduct annual surveys of veteran-owned small businesses applying for SBA Patriot Express Loans similar to the annual survey the SBA currently sponsors for small businesses receiving services from the SBA's management and training programs.¹²³

Small Loan Advantage and Community Advantage Programs

The Small Loan Advantage and Community Advantage programs became operational on February 15, 2011.¹²⁴ They are designed to increase lending to underserved low- and moderate-income communities. Both programs offer a streamlined application process for loans up to \$250,000. The two programs replaced the Community Express Pilot Program, which was also designed to increase lending to underserved communities. It was created by the SBA in May 1999, and ended on April 30, 2011.¹²⁵

The Small Loan Advantage program "is structured to encourage larger, existing SBA lenders to make lower-dollar loans, which often benefit businesses in underserved markets."¹²⁶ It provides the same loan guaranty as the 7(a) program on loan amounts up to \$250,000 (85% for loans up to \$150,000 and 75% for those greater than \$150,000). The loan proceeds can be used for the same purposes as the 7(a) program (expansion, renovation, new construction, the purchase of land or buildings, the purchase of equipment, fixtures, and lease-hold improvements, working capital, to

¹²¹ Ibid.

¹²² In FY2010, the SBA's Veterans Business Outreach Centers Program, which provides management and technical assistance training for veteran-owned small businesses, conducted its sixth annual "Customer Satisfaction Survey." The centers surveyed 1% of their total veteran customer population (408 of the 485 clients surveyed responded). The FY2010 survey found that 85% of the clients using the centers were satisfied or highly satisfied with the quality, relevance and timeliness of the assistance provided. Clients evaluating the centers gave 85% ratings for the training programs provided and 85% ratings for program evaluation. See U.S. Small Business Administration, "FY2012 Congressional Budget Justification and FY2010 Annual Performance Report," Washington, DC, p. 73.

¹²³ For further information and analysis, see CRS Report R41352, *Small Business Management and Technical Assistance Training Programs*, by Robert Jay Dilger; U.S. Small Business Administration, Office of Entrepreneurial Development, "Impact Study of Entrepreneurial Development Resources," Washington, DC, September 13, 2010, <http://www.sba.gov/sites/default/files/09-10%20SBA%20ED%20Resources%20Impact%20Study%20Final%20Report.pdf>; and P.L. 96-302, the Small Business Development Center Act of 1980.

¹²⁴ U.S. Small Business Administration, "Small Loan Advantage," Washington, DC, <http://www.sba.gov/content/small-loan-advantage>; and U.S. Small Business Administration, "SBA Announces New Initiatives Aimed at Increasing Lending in Underserved Communities," Washington, DC, December 15, 2010, <http://www.sba.gov/content/sba-announces-new-initiatives-aimed-increasing-lending-underserved-communities>.

¹²⁵ U.S. Congress, House Committee on Small Business, *Small Business Financing and Investment Act Of 2009*, report to accompany H.R. 3854, 111th Cong., 2nd sess., October 26, 2009, H.Rept. 111-315 (Washington: GPO, 2009), p. 7. The SBA indicated that the Community Express Pilot Program "has had mixed outcomes," providing loans "to new businesses, minority businesses and other underserved sectors" but with "significantly higher default rates (almost 40% of loans defaulted in certain cohorts) compared with other similarly sized 7(a) loans." See U.S. Small Business Administration, "Community Express Pilot Program," *75 Federal Register* 80562, December 22, 2010.

¹²⁶ U.S. Small Business Administration, "Advantage Loan Initiatives," Washington, DC, <http://www.sba.gov/advantage>.

refinance debt for compelling reasons, seasonal line of credit, and inventory). The loan terms and guaranty fees are also the same as the 7(a) program.¹²⁷ The program's interest rates are negotiable with the lender, subject to the same maximum rate limitations as the 7(a) program.¹²⁸

The program is available to lenders participating in the SBA's Preferred Lender Program (about 545 lenders, including most of the SBA's highest volume lenders). These lenders are authorized to use expedited loan processing procedures, which include a two-page application for borrowers and allow lenders to use their own note and guaranty agreements. Most Small Loan Advantage loans are expected "to be approved in a matter of minutes through electronic submission" or "within 5 to 10 days" otherwise.¹²⁹

The Community Advantage pilot program is designed to increase lending in underserved communities by increasing "the number of SBA 7(a) lenders who reach underserved communities, targeting community-based, mission-focused financial institutions which were previously not able to offer SBA loan."¹³⁰ These mission-focused financial institutions include "Community Development Financial Institutions, SBA's Certified Development Companies and SBA's nonprofit microlending intermediaries."¹³¹ They are expected "to maintain at least 60% of their SBA loan portfolio in underserved markets, including loans to small businesses in, or that have more than 50% of their workforce residing in, low-to-moderate income (LMI) communities; in Empowerment Zones and Enterprise Communities; in HUBZones; start-ups (firms in business less than 2 years); and veteran-owned businesses and those that would be eligible for Patriot Express."¹³²

The Community Advantage program is a three-year pilot program that provides the same loan guaranty as the 7(a) program on loan amounts up to \$250,000 (85% for loans up to \$150,000 and 75% for those greater than \$150,000). The loan proceeds can be used for the same purposes as the 7(a) program (expansion, renovation, new construction, the purchase of land or buildings, the purchase of equipment, fixtures, and lease-hold improvements, working capital, to refinance debt for compelling reasons, seasonal line of credit, and inventory). The loan terms and guaranty fees are also the same as the 7(a) program.¹³³ The loan's maximum interest rate is prime, plus 4%.¹³⁴ The program has an expedited approval process which includes a two-page application for borrowers and a goal of completing the loan approval process within 5 to 10 days.¹³⁵

The SBA has indicated that the Community Advantage program's goal is to "leverage the experience these institutions already have in lending to minority, women-owned and start-up

¹²⁷ U.S. Small Business Administration, "Small Loan Advantage," Washington, DC, <http://www.sba.gov/content/small-loan-advantage>.

¹²⁸ *Ibid.*

¹²⁹ *Ibid.*

¹³⁰ U.S. Small Business Administration, "Advantage Loan Initiatives," Washington, DC, <http://www.sba.gov/advantage>.

¹³¹ *Ibid.*

¹³² *Ibid.*

¹³³ *Ibid.*

¹³⁴ U.S. Small Business Administration, "Community Advantage Participant Guide," Washington, DC, p. 18, <http://www.sba.gov/sites/default/files/files/CA%20-%20Participants%20Guide.pdf>

¹³⁵ U.S. Small Business Administration, "Community Advantage," Washington, DC, <http://www.sba.gov/content/community-advantage>.

companies in economically challenged markets, along with their management and technical assistance expertise, to help make their borrowers successful.”¹³⁶

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¹³⁶ U.S. Small Business Administration, “SBA Announces New Initiatives Aimed at Increasing Lending in Underserved Communities,” Washington, DC, December 15, 2010, <http://www.sba.gov/content/sba-announces-new-initiatives-aimed-increasing-lending-underserved-communities>. The SBA maintains a list of approved Community Advantage pilot program lenders on its website at <http://www.sba.gov/content/community-advantage-approved-lenders>.