



**Congressional
Research Service**

Informing the legislative debate since 1914

Small Business Administration 7(a) Loan Guaranty Program

Robert Jay Dilger

Senior Specialist in American National Government

July 1, 2015

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 program. Its name is derived 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 and loan guaranties to American small businesses.

In FY2014, the SBA approved 52,044 7(a) loans totaling \$19.2 billion. The average approved 7(a) loan amount was \$368,737. Proceeds from 7(a) loans may be used to establish a new business or to assist in the operation, acquisition, or expansion of an existing business.

Congressional interest in the 7(a) program has increased in recent years because of concerns that small businesses might be prevented from accessing sufficient capital to enable them to assist in the economic recovery. Some, including President Obama, argue that the SBA should 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 create jobs. Others worry about the long-term adverse economic effects of spending programs that increase the federal deficit. They advocate business tax reduction, financial credit market reforms, and fiscal restraint as the best means to help small businesses further economic growth and job creation.

This report discusses 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 proceeds, borrower satisfaction, and borrower demographics. It 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.

In addition, the report surveys congressional action taken during the 111th Congress to enhance small businesses’ access to capital, including providing more than \$1.1 billion to temporarily subsidize the 7(a) and 504/Certified Development Companies (CDC) loan guaranty programs’ fees and temporarily increase the 7(a) program’s maximum loan guaranty percentage to 90% (funding was exhausted on January 3, 2011); raising the 7(a) program’s gross loan limit from \$2 million to \$5 million; and establishing an alternative size standard for the 7(a) and 504/CDC loan programs.

This report also discusses the Obama Administration’s decision to waive the up-front loan guaranty fee and ongoing servicing fee for 7(a) loans of \$150,000 or less approved in FY2014 and FY2015; the up-front, one-time loan guaranty fee for veteran loans under the SBAExpress program (up to \$350,000) from January 1, 2014, through the end of FY2015 (called the Veterans Advantage Program); and 50% of the up-front loan guaranty fee on all non-SBAExpress 7(a) loans to veterans exceeding \$150,000 in FY2015. It also examines legislation introduced during the 114th Congress (H.R. 2499, the Veterans Entrepreneurship Act of 2015, and S. 957, the Veterans Entrepreneurship Act) to authorize and make permanent the up-front, one-time loan guaranty fee for veteran loans under the SBAExpress program.

The **Appendix** to this report provides a brief description of the 7(a) program’s SBAExpress, Export Express, and Community Advantage programs.

Contents

Small Business Administration Loan Guaranty Programs.....	1
Borrower Eligibility Standards and Program Requirements.....	4
Borrower Eligibility Standards.....	4
Borrower Program Requirements.....	5
Use of Proceeds.....	5
Loan Amounts.....	5
Loan Terms, Interest Rate, and Collateral.....	6
Lender Eligibility Standards and Program Requirements.....	7
Lender Eligibility Standards.....	7
CLP and PLP Lenders.....	8
Lender Program Requirements.....	9
The Application Process.....	9
SBA Guaranty and Servicing Fees.....	13
Lender Packaging, Servicing, and Other Fees.....	16
Program Statistics.....	17
Loan Volume.....	17
Appropriations for Loan Subsidy Costs.....	19
Administrative Expenses.....	20
Use of Proceeds and Borrower Satisfaction.....	20
Borrower Demographics.....	21
Congressional Issues.....	22
Access to Capital.....	22
Program Administration.....	23
Oversight of 7(a) Lenders.....	23
Outcome-Oriented Performance Measures.....	28
Legislative Activity During the 111 th Congress.....	30
The Obama Administration’s Proposals.....	30
Arguments for Increasing the SBA’s Maximum Loan Limits.....	30
Arguments Against Increasing the SBA’s Maximum Loan Limits.....	31
P.L. 111-5, the American Recovery and Reinvestment Act of 2009 (ARRA).....	31
P.L. 111-240, the Small Business Jobs Act of 2010.....	32
Legislative Activity During the 112 th Congress.....	33
Legislative Activity During the 113 th Congress.....	33
Legislative Activity During the 114 th Congress.....	34
Concluding Observations.....	34

Tables

Table 1. SBA Annual Service and Guaranty Fees, FY2013-FY2015.....	15
Table 2. 7(a) Loan Guaranty Program, Loan Volume, FY2007-FY2014.....	17
Table 3. Business Loan Credit Subsidies, 7(a) and 504/CDC Loan Guaranty Programs, FY2007-FY2016.....	20

Appendixes

Appendix. 7(a) Specialized Programs..... 36

Contacts

Author Contact Information..... 40

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 Its name is derived 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.

The SBA also administers several 7(a) subprograms that offer streamlined and expedited loan procedures for particular groups of borrowers, including the SBAExpress, 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.³

Proceeds from 7(a) loans may be used to establish a new business or to assist in the operation, acquisition, or expansion of an existing business. Specific uses include to acquire land (by purchase or lease); improve a site (e.g., grading, streets, parking lots, and landscaping); purchase, 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.⁴

In FY2014, the SBA approved 52,044 7(a) loans totaling \$19.2 billion.⁵ As will be discussed, the total number and amount of SBA 7(a) loans approved (and actually disbursed) declined in FY2008 and FY2009, increased during FY2010 and FY2011, declined somewhat in FY2012, and increased in FY2013 and FY2014.

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

¹ U.S. Small Business Administration (SBA), *Fiscal Year 2010 Congressional Budget Justification*, 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 SBA, “Small Loan Advantage and Community Advantage 7(a) Loan Initiatives,” at <https://www.sba.gov/offices/headquarters/oca/resources/14836>. The SBA also administers several special purpose loan guaranty programs that address particular business needs, including the Export Express Loan Program, International Trade Loan Program, Export Working Capital Program, the Community Adjustment and Investment Program (CAIP), CAPLines Program, Employee Trusts Program, and Pollution Control Program. The Pollution Control Program is currently not funded. See SBA, “Special Purpose Loans Program,” at <https://www.sba.gov/category/navigation-structure/loans-grants/small-business-loans/sba-loan-programs/7a-loan-program/special-purpose-loans-program>.

⁴ 13 C.F.R. §120.120.

⁵ SBA, “SBA Lending Statistics for Major Programs (as of 9/30/2014),” at https://www.sba.gov/sites/default/files/aboutsbaarticle/WebsiteReport_asof9_30_2014.pdf. The number of 7(a) loans approved annually is typically about 10% to 20% higher than the number of loans disbursed (e.g., some borrowers decide not to accept the loan or there is a change in business ownership). The amount of 7(a) loans approved annually is typically about 10% to 15% higher than the amount disbursed. In FY2013, the SBA approved 46,399 7(a) loans amounting to more than \$17.8 billion. In FY2012, the SBA approved 44,377 7(a) loans amounting to more than \$15.1 billion.

to obtain access to sufficient capital and credit.⁶ Congressional interest in the 7(a) loan program has increased in recent years because of concerns that small businesses might be prevented from accessing sufficient capital to enable them to assist in the economic recovery.

Some, including President Obama, argue that the SBA should 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 create jobs. Others worry about the long-term adverse economic effects of spending programs that increase the federal deficit. They advocate business tax reduction, reform of financial credit market regulation, and federal fiscal restraint as the best means to help small businesses further economic growth and job creation.

This report discusses 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 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 then surveys congressional action taken during the 111th Congress to provide the SBA additional resources to help small businesses gain greater access to capital. For example,

- P.L. 111-5, the American Recovery and Reinvestment Act of 2009 (ARRA), provided the SBA an additional \$730 million, including \$375 million to temporarily subsidize the 7(a) and 504/ Certified Development Companies (CDC) loan guaranty programs' fees (\$299 million) and to temporarily increase the 7(a) program's maximum loan guaranty percentage to 90% (\$76 million).⁷
- P.L. 111-240, the Small Business Jobs Act of 2010, provided \$505 million (plus \$5 million for administrative expenses) to extend the fee subsidies and 90% loan guaranty percentage through December 31, 2010; increased the 7(a) program's gross loan limit from \$2 million to \$5 million; and established an alternative size standard for the 7(a) and 504/CDC loan programs to enable more small businesses to qualify for assistance.
- 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).

In addition, this report discusses three bills introduced during the 112th Congress that would have changed the 7(a) program. S. 1828, a bill to increase small business lending (and for other purposes) would have reinstated for one year following the date of its enactment the fee subsidies for the 7(a) and 504/CDC loan guaranty programs and the 90% loan guaranty percentage for the

⁶ U.S. Government Accountability Office (GAO), *Small Business Administration: 7(a) Loan Program Needs Additional Performance Measures*, GAO-08-226T, November 1, 2007, pp. 3, 9-11, at <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, at http://www.aei.org/files/2006/04/13/20060414_wp126.pdf. Proponents of federal funding for the SBA's loan guarantee programs also argue that small businesses can promote competitive markets. See P.L. 83-163, §2(a), as amended; and 15 U.S.C. §631a.

⁷ SBA, "Recovery Act Agency Plan," May 15, 2009, at https://www.sba.gov/sites/default/files/recovery_act_reports/sba_recovery_act_plan.pdf.

7(a) program, which were originally authorized by ARRA. H.R. 2936, the Small Business Administration Express Loan Extension Act of 2011, would have extended a one-year increase in the maximum loan amount for the SBAExpress program from \$350,000 to \$1 million for an additional year. That temporary increase was authorized by P.L. 111-240 and expired on September 27, 2011. S. 532, the Patriot Express Authorization Act of 2011, would have provided statutory authorization for the Patriot Express Pilot Program and increased its loan guaranty percentages and its maximum loan amount from \$500,000 to \$1 million. The Patriot Express Pilot Program was subsequently discontinued by the SBA on December 31, 2013.

This report also discusses the Obama Administration's decision to waive the up-front loan guaranty fee and ongoing servicing fee for 7(a) loans of \$150,000 or less approved in FY2014 and FY2015. During the 113th Congress, H.R. 2462, the Small Business Opportunity Acceleration Act of 2013, would have made this fee waiver permanent.

In addition, the Administration has decided to waive the up-front, one-time loan guaranty fee for veteran loans under the SBAExpress program (up to \$350,000) from January 1, 2014, through the end of FY2015 (called the SBA Veterans Advantage Program).⁸ The Administration is also waiving 50% of the up-front loan guaranty fee on all non-SBAExpress 7(a) loans to veterans exceeding \$150,000 in FY2015.⁹

There have been several legislative efforts to statutorily authorize or make permanent the Veterans Advantage Program. During the 113th Congress, S. 2143, the Veterans Entrepreneurship Act, would have authorized the fee waiver and made it permanent. P.L. 113-235, the Consolidated and Further Continuing Appropriations Act, 2015, provided statutory authorization to waive the 7(a) SBAExpress program's guarantee fee for veterans (and their spouses) in FY2015. During the 114th Congress, the Veterans Entrepreneurship Act was reintroduced on April 15, 2015 (S. 957). In addition, H.R. 2499, the Veterans Entrepreneurship Act of 2015, introduced on May 21, 2015, would authorize the fee waiver and make it permanent, subject to the 7(a) loan guaranty program, in its entirety, not having a subsidy cost.¹⁰ On June 10, 2015, the Senate Committee on Small Business and Entrepreneurship reported S. 957 and the House Committee on Small Business reported H.R. 2499.

The **Appendix** to this report provides a brief description of the 7(a) program's SBAExpress, Export Express, and Community Advantage programs.

⁸ The small business must be owned and controlled (51%+) by one or more of the following groups: veteran, active duty military in the Transition Assistance Program, reservist or National Guard member, a spouse of any of these groups, or a widowed spouse of a servicemember or veteran who died during service or of a service-connected disability.

⁹ SBA, "SBA Information Notice: SBA Veterans Advantage – Renewal and Expansion of Fee Relief," September 19, 2014, at https://www.sba.gov/sites/default/files/lender_notices/5000-1319.pdf.

¹⁰ U.S. Congress, House Committee on Small Business, *Veterans Entrepreneurship Act of 2015*, report to accompany H.R. 2499, 114th Cong., 1st sess., June 25, 2015, H.Rept. 114-187 (Washington: GPO, 2015), p. 9.

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;¹¹
- 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 nonfederal sources without SBA assistance.¹²

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

- character, reputation, and credit history;
- experience and depth of management;
- 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.¹³

¹¹ For further analysis, see CRS Report R40860, *Small Business Size Standards: A Historical Analysis of Contemporary Issues*, by Robert Jay Dilger.

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

¹³ 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.¹⁴

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.¹⁵

Loan Amounts

As mentioned previously, P.L. 111-240 increased the 7(a) program's maximum gross loan amount for any one 7(a) loan from \$2 million to \$5 million (up to \$3.75 million maximum guaranty). In FY2014, the average approved 7(a) loan amount was \$368,737.¹⁶

¹⁴ 13 C.F.R. §120.120.

¹⁵ 13 C.F.R. §120.130; and SBA, "Use of 7(a) Loan Proceeds," at <http://www.sba.gov/content/use-7a-loan-proceeds>.

¹⁶ SBA, "SBA Lending Statistics for Major Programs (as of 9/30/2014)," at https://www.sba.gov/sites/default/files/aboutsbaarticle/WebsiteReport_asof9_30_2014.pdf.

Loan Terms, Interest Rate, and Collateral

Loan Terms

A 7(a) loan is 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 multistep 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 June 2015 for 7(a) loans with maturities of less than seven years are 7.41% for loans greater than \$50,000, 8.41% for loans over \$25,000 but not exceeding \$50,000, and 9.41% for loans of \$25,000 or less. The maximum allowable fixed interest rates in June 2015 for 7(a) loans with maturities of seven years or more are 7.91% for loans greater than \$50,000, 8.91% for loans over \$25,000 but not exceeding \$50,000, and 9.91% for loans of \$25,000 or less.²⁰

The 7(a) program's maximum allowable variable interest rate may be pegged to the lowest prime rate (3.25% in June 2015), the 30-day LIBOR rate plus 300 basis points (3.18% in June 2015), or the SBA optional peg rate (2.250% in the fourth quarter of FY2015).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

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 SBA, “Business Loan Program Maximum Allowable Fixed Rate,” 74 *Federal Register* 50263-50264, September 30, 2009.

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

²¹ *Ibid*; and SBA, “Welcome Lenders,” at <https://www.sba.gov/for-lenders>.

²² SBA, “7(a) Loan Program: Terms and Conditions,” at <https://www.sba.gov/offices/headquarters/oca/resources/13022>.

Collateral

For 7(a) loans of \$25,000 or less, the SBA does not require lenders to take collateral. For 7(a) loans exceeding \$25,000 to \$350,000, the lender must follow the collateral policies and procedures that it has established and implemented for its similarly sized non-SBA-guaranteed commercial loans. However, the lender must, at a minimum, obtain a first lien on assets financed with loan proceeds, and a lien on all of the applicant's fixed assets to secure the loan. For 7(a) loans exceeding \$350,000, the SBA requires lenders to collateralize the loan to the maximum extent possible up to the loan amount.²³ If business assets do not fully secure the loan, the lender must take available equity in the principal's personal real estate (residential and investment) as collateral.²⁴

7(a) loans are considered "fully secured" if the lender has taken security interests in all available fixed assets with a combined "net book value" up to the loan amount.²⁵ The SBA directs lenders to not decline a loan solely on the basis of inadequate collateral because "one of the primary reasons lenders use the SBA-guaranteed program is for those Small Business Applicants that demonstrate repayment ability but lack adequate collateral to fully repay the loan if the loan defaults."²⁶

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 the SBA. They must also maintain satisfactory performance, as determined by the 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.²⁷ In FY2014, 2,244 lenders provided 7(a) loans.²⁸

²³ SBA, "SOP 50 10 5(H): Lender and Development Company Loan Programs," (effective May 1, 2015), p. 167, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

²⁴ Ibid.

²⁵ Ibid., p. 166. "Net book value" is defined as an asset's original price minus depreciation and amortization. New machinery and equipment may be valued at 75% of Net Book Value, or 80% with an Orderly Liquidation Appraisal minus any prior liens for the calculation of "fully-secured." Used or existing machinery and equipment may be valued at 50% of Net Book Value or 80% with an Orderly Liquidation Appraisal minus any prior liens for the calculation of "fully-secured." Real estate can be valued supported at 85% of the value for the calculation of "fully-secured." If the loan will be secured by the fixed assets and the valuation of fixed assets is greater than their depreciated value (net book value), an independent appraisal by a qualified individual must be obtained by the lender to support the higher valuation.

²⁶ Ibid., p. 165.

²⁷ 13 C.F.R. §120.410.

²⁸ SBA, *Fiscal Year 2016 Congressional Budget Justification and FY 2014 Annual Performance Report*, p. 42. There (continued...)

CLP and PLP Lenders

The SBA established the Certified Lenders Program (CLP) on February 26, 1979, initially on a six-month pilot basis.²⁹ It is designed to provide expeditious service on 7(a) loan applications received from lenders who have a successful SBA lending track record and a thorough understanding of SBA policies and procedures. CLP lenders submit the same application forms and documentation required of standard 7(a) loan packages. They must also prepare a draft of the SBA Authorization (of loan guaranty approval). The SBA loan reviewer “relies heavily on the information the lender provides.”³⁰ If the lender’s presentation is not adequate for CLP processing, the SBA may convert the application from CLP processing to standard loan processing. In recent years, CLP lenders have approved about 1.0% of the number of 7(a) loans approved each year and 2.4% of the amount of 7(a) loans approved each year.³¹

The SBA started the Preferred Lenders Program (PLP) on March 1, 1983, initially on a pilot basis.³² It 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.³³ PLP loan approvals are subject only to a brief eligibility review and the assignment of a loan number by SBA.³⁴ PLP lenders draft the SBA Authorization (of loan guaranty approval) without the SBA’s review, and execute it on behalf of the SBA. In recent years, PLP lenders have approved about 27.2% of the number of 7(a) loans approved each year and about 56.8% of the amount of 7(a) loans approved each year.³⁵

PLP lenders must comply with all of the SBA’s business loan eligibility requirements, credit policies, and procedures. The PLP lender is required to stay informed on, and apply, all of the SBA’s loan program requirements. They must also complete and retain in the lender’s file all forms and documents required of standard 7(a) loan packages.³⁶

(...continued)

were 2,345 active 7(a) lenders in FY2013, and 2,476 active 7(a) lenders in FY2012.

²⁹ U.S. Congress, Senate Select Committee on Small Business, *SBA Loan Oversight*, hearing on SBA loan oversight, 96th Cong., 1st sess., September 18, 1997 (Washington: GPO, 1997), p. 31; and U.S. General Accounting Office, *SBA’s Pilot Programs to Improve Guaranty Loan Procedures Need Further Development*, CED-81-25, February 2, 1981, p. 7, at <http://www.gao.gov/assets/140/131789.pdf>; and U.S. General Accounting Office, *SBA’s Certified Lenders Program Falls Short of Expectations*, RCED-83-99, June 7, 1983, p. 1, at <http://www.gao.gov/assets/150/140126.pdf>.

³⁰ SBA, “SOP 50 10 5(H): Lender and Development Company Loan Programs,” (effective May 1, 2015), p. 19, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

³¹ SBA, Office of Congressional and Legislative Affairs, correspondence with the author, November 21, 2013.

³² U.S. General Accounting Office, *SBA’s Certified Lenders Program Falls Short of Expectations*, RCED-83-99, June 7, 1983, p. 3, at <http://www.gao.gov/assets/150/140126.pdf>.

³³ U.S. General Accounting Office, *Small Business: Analysis of SBA’s Preferred Lenders Program*, GAO/RCED-92-124, May 15, 1992, pp. 1-4, <http://www.gao.gov/assets/220/216229.pdf>.

³⁴ SBA, “SOP 50 10 5(H): Lender and Development Company Loan Programs,” (effective May 1, 2015), pp. 21-22, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

³⁵ PLP lenders approved 12,570 7(a) loans totaling \$11.7 billion in FY2014, 13,457 7(a) loans totaling \$10.4 billion in FY2013, 12,472 7(a) loans totaling \$8.4 billion in FY2012, and 15,228 7(a) loans totaling \$10.7 billion in FY2011. See SBA, “SBA Lending Statistics for Major Programs (as of 9/30/2014),” at https://www.sba.gov/sites/default/files/aboutsbaarticle/WebsiteReport_asof9_30_2014.pdf.

³⁶ SBA, “SOP 50 10 5(H): Lender and Development Company Loan Programs,” (effective May 1, 2015), pp. 28-29, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

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 require 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 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.

If the lender determines that it is willing to provide the loan, but only with an SBA guaranty, it submits the application for approval to the SBA's Loan Guaranty Processing Center (LGPC) through the SBA's E-Tran (Electronic Loan Processing/Servicing) website or, if attachments to the application are too large for E-Tran, by secured electronic file transfer. The LGPC has two physical locations: Citrus Heights, CA, and Hazard, KY.³⁷ 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.³⁸ The SBA has authorized PLP and express lenders to make credit decisions without SBA review prior to loan approval. However, the PLP and express lender's analysis is subject to the SBA's review and determination of adequacy when the lender requests the SBA to purchase its guaranty and when the SBA is conducting a review of the lender.³⁹

As an additional safeguard against the potential for loan defaults, the SBA now requires all non-express 7(a) loans of \$350,000 or less to be SBA credit scored through E-Tran prior to submission/approval.⁴⁰

- If the credit score is below the minimum set by the SBA, the loan may only be submitted as a standard 7(a) application or as an SBAExpress loan (for a 50% guaranty) if the lender is a SBAExpress lender.

³⁷ Ibid., p. 195.

³⁸ GAO, *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, at <http://www.gao.gov/new.items/d08995.pdf>.

³⁹ SBA, "SOP 50 10 5(H): Lender and Development Company Loan Programs," (effective May 1, 2015), p. 163, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

⁴⁰ The SBA's credit scoring requirement was initially required of Small Loan Advantage loans, effective June 1, 2012. See SBA, "SBA Information Notice 5000 – 1240: Revised and Expanded Small Loan Advantage – Changes Incorporated into SOP 50 10 5(E)," May 25, 2012, at <https://www.sba.gov/content/revised-and-expanded-small-loan-advantage-changes-incorporated-sop-50-10-5e>. The SBA's credit scoring requirement was expanded to all non-express 7(a) loans of \$350,000 or less on January 1, 2014. See SBA, "SOP 50 10 5(F): Lender and Development Company Loan Programs," (effective January 1, 2014), p. 161, at <https://www.sba.gov/sites/default/files/Clean%20FINAL%20SOP%2050%2010%205%20%28F%29.pdf>. The SBA calculates the credit score based on a combination of consumer credit bureau data, business bureau data, borrower financials, and application data. The minimum acceptable credit score is based on the lower end of the risk profile of the current SBA portfolio and may be adjusted up or down from time to time.

- If the credit score is acceptable to the SBA, the lender is a PLP lender, and the loan is eligible to be processed under the PLP lender's delegated authority, the lender will receive an SBA loan number indicating that the loan is approved.⁴¹ The PLP lender's documentation, including underwriting, closing, and servicing, must be maintained in their files, and can be reviewed by the SBA at any time.
- If the lender is not a PLP lender or if the loan is not eligible to be submitted under the PLP lender's delegated authority, E-Tran will generate a message instructing the lender to send application forms, along with the SBA loan application number provided by E-Tran, to the LGPC for processing.⁴²

The application materials required for a SBA guaranty vary depending on the size of the loan (\$350,000 or less versus exceeding \$350,000) and the method of processing used by the lender (standard versus expedited/express).

Application packages “must include the forms and documentation the lender requires in order to make an informed eligibility and credit decision” and the information provided must “be certified by the applicant as true and complete.”⁴³ The following SBA documentation is required for all 7(a) standard loans of \$350,000 or less:

- *Form 1919: Borrower Information Form.* SBA form 1919 provides information about the borrower (name, name of business, social security number, date and place of birth, gender, race, veteran, etc.); the loan request; any indebtedness; the principals and affiliates; current or previous government financing; the applicant's eligibility (e.g., criminal information, citizenship status); the loan's eligibility for delegated or expedited processing (e.g., the borrower is not more than 60 days delinquent in child support payments, not proposed or presently excluded from participation in this transaction by any federal department or agency, has no potential for a conflict of interest due to an owner being a current or former SBA employee, a Member of Congress, a SCORE volunteer, etc.), and, among other disclosures, the firm's existing number of employees, the number of jobs to be created as a result of the loan, and the number of jobs that will be retained as a result of the loan that would have otherwise been lost.⁴⁴
- *Form 912: Statement of Personal History.* SBA form 912 is required if the borrower reports on Form 1919 an arrest in the past six months for a criminal offense or had ever been convicted, plead guilty, plead nolo contendere, been placed on pretrial diversion, or been placed on any form of parole or probation (including probation before judgment) of any criminal offense.⁴⁵ Form 912

⁴¹ If the PLP lender indicates that the loan is eligible to be processed under the PLP lender's delegated authority, the lender is also certifying that SBA Form 1920 has been completed, signed, dated, and filed in the loan file.

⁴² Ibid., p. 203.

⁴³ Ibid., pp. 196-197.

⁴⁴ SBA, “SBA Form 1919: Borrower Information Form for use with all 7(a) Programs,” at https://www.sba.gov/sites/default/files/forms/SBA%201919_SSN_1.PDF.

⁴⁵ SBA, “SBA Form 912: Statement of Personal History,” at <https://www.sba.gov/sites/default/files/forms/SBA%20Form%20912%20202-13.pdf>. The lender is required to process a background check and character determination if the borrower has been arrested in the past six months for any criminal offense or if the borrower has ever been convicted, plead guilty, plead nolo contendere, been placed on pretrial diversion, or been placed on any form of parole or probation (including probation before judgment) of any criminal offense

requires the borrower to furnish details concerning his or her offense(s) and authorizes the SBA's Office of Inspector General to request criminal record information about the applicant from criminal justice agencies for determining program eligibility. It must be dated within 90 days of the application's submission to the SBA.

- *Form 159: Fee Disclosure and Compensation Agreement.* SBA form 159 is required if the borrower reports on Form 1919 that he or she used (or intends to use) a packager, broker, accountant, lawyer, etc. to assist in preparing the loan application or any related materials.⁴⁶ SBA form 159 is also required if the lender retains the services of a packager, broker, accountant, lawyer, etc. to assist in preparing the loan application or any related materials. Form 159 provides identifying information about the packager, broker, accountant, lawyer, etc. and the fees paid to any such person.
- *Form 601: Agreement of Compliance* (prohibiting discrimination). SBA form 601 is required if the borrower reports on Form 1919 that more than \$10,000 of the loan proceeds will be used for construction.⁴⁷ Form 601 certifies that the borrower will cooperate actively in obtaining compliance with Executive Order 11246, which prohibits discrimination on the basis of race, color, religion, sex, or national origin and requires affirmative action to ensure equality of opportunity in all aspects of employment related to federally assisted construction projects in excess of \$10,000.
- *Form 1920: Lenders Application for Guaranty for all 7(a) Programs.*⁴⁸ SBA form 1920 provides identifying information about the lender; the loan type (standard, SBAExpress, Export Express, etc.); loan terms; use of proceeds; the business's size and information about affiliates, if any; the applicant's character; if credit is reasonably available elsewhere; the type of business; potential conflicts of interest; and other information such the number of jobs created or retained. PLP lenders complete the form and retain it in the loan file. Other lenders must submit this form electronically to the LGPC.
- *Verification of Alien Status.* Documentation of the U.S. Citizenship and Immigration Services (USCIS) status of each alien is required prior to submission of the application to the SBA.
- *Lender's Credit Memorandum.* For loans up to and including \$350,000, the Lender's Credit Memorandum includes a brief description of the history of the business and its management; the debt service coverage ratio (net operating income compared to total debt service must be at least 1:1); statement that the lender has reconciled financial data (including seller's financial data) against IRS transcripts; an owner/guarantor analysis (including personal financial condition); lender's discussion of life insurance requirements; explanation and justification for any refinancing; analysis of credit, including lender's rationale for

⁴⁶ SBA, "SBA Form 159: Fee Disclosure and Compensation Agreement," at https://www.sba.gov/sites/default/files/forms/SBA_159_7a.pdf.

⁴⁷ SBA, "SBA Form 601: Agreement of Compliance," at <https://www.sba.gov/sites/default/files/forms/SBA%20601.pdf>.

⁴⁸ SBA, "SBA Form 1920: Lenders Application for Guaranty for all 7(a) Programs," at https://www.sba.gov/sites/default/files/forms/SBA%201920_1.pdf.

recommending approval; for a change of ownership, discussion/analysis of business valuation and how the change benefits the business; discussion of any liens, judgments or bankruptcy filings; and discussion of any other relevant information. For loans exceeding \$350,000, the Lender's Credit Memorandum must also include an analysis of collateral and a financial analysis which includes an analysis of the historical financial statements; defining assumptions supporting projected cash flow; and, when used, spread of pro-forma balance sheet, ratio calculations, and working capital analysis.⁴⁹

- *Cash Flow Projections.* A projection of the borrower's cash flow, month-by-month for one year, is required for all new businesses, and when otherwise applicable.

The following forms and documentation are also required for 7(a) standard loans exceeding \$350,000:

- *Form 413: Personal Financial Statement.* SBA form 413 provides detailed information concerning the applicant's assets and liabilities and must be 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. Lenders may substitute their own Personal Financial Statement form.
- *Form 1846: Statement Regarding Lobbying.* SBA Form 1846 must be signed and dated by lender.⁵⁰ It indicates that if any funds have been paid or will be paid to any person for influencing or attempting to influence an officer or employee of any agency, Member of Congress, an officer or employee of Congress, or an officer or employee of a Member of Congress in connection with this commitment, the lender will complete and submit a Standard Form LLL "Disclosure of Lobbying Activities."⁵¹
- A copy of *Internal Revenue Service (IRS) Form 4506-T, Request for Copy of Tax Return.* Lenders must identify the date IRS Form 4506-T was sent to the IRS. For non-delegated lenders, verification of IRS Form 4506-T is required prior to submission of the application to the SBA. For PLP and express lenders, verification of IRS Form 4506-T is required prior the first disbursement.
- *Business Financial Statements* and/or tax returns dated within 180 days of the application's 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, and (5) interim profit and loss statements.
- *Affiliate and Subsidiary Financial Statements* and/or tax returns dated within 180 days of the application's submission to the SBA, consisting of (1) year-end

⁴⁹ SBA, "Standard 7(a) LGPC 10-Tab Submission Instructions," at https://www.sba.gov/sites/default/files/files/LGPC%2010-Tab%20Template_20140313.pdf.

⁵⁰ SBA, "SBA Form 1846: Statement Regarding Lobbying," at https://www.sba.gov/sites/default/files/forms/bank_sba1846.pdf.

⁵¹ U.S. Office of Management and Budget, "Standard Form LLL: Disclosure of Lobbying Activities," at <https://www.whitehouse.gov/sites/default/files/omb/grants/sfllin.pdf>.

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, and (5) interim profit and loss statements.

- A copy of the *Lease Agreement*, if applicable.
- A detailed *Schedule of Collateral*.⁵²
- A detailed *List of M&E* (machinery and equipment) being purchased with SBA loan proceeds, including cost quotes.
- If real estate is to be purchased with the loan proceeds, a *Real Estate Appraisal*, *Environmental Investigation Report* questionnaire, a cost breakdown, and copy of any *Real Estate Purchase Agreements*.
- If purchasing an existing business with loan proceeds, a (1) copy of buy-sell agreement, (2) copy of business valuation, (3) pro forma balance sheet for the business being purchased as of the date of transfer, (4) copy of the seller's financial statements for the last three complete fiscal years or for the number of years in business if less than three years, (5) interim statements no older than 180 days from date of submission to the SBA, and (6) if the seller's financial statements are not available, the seller must provide an alternate source of verifying revenues.
- An explanation of the type and source of applicant's equity injection. Proper evidence of a borrower's equity injection may include the copy of a check together with proof it was processed, or a copy of an escrow settlement sheet with a bank account statement showing the injection into the business prior to disbursement. A promissory note, "gift letter," or financial statement is generally not sufficient evidence.⁵³
- If the borrower is a franchise and is listed on <http://www.franchiseregistry.com>, a certification of franchise documents is required. If the franchise is not listed on the registry, a copy of the Franchise Agreement and Federal Trade Commission Disclosure Report of Franchisor must be submitted.⁵⁴

SBA Guaranty and Servicing Fees

To offset its costs, the SBA is authorized to charge lenders an up-front, one-time guaranty fee and an annual, ongoing service fee for each 7(a) loan approved and disbursed.⁵⁵ The SBA's fees vary depending on loan amount and loan maturity. The maximum guaranty fee for 7(a) loans with maturities exceeding 12 months is set by statute and varies depending on the loan amount.⁵⁶ The

⁵² For loans of up to \$350,000, if a schedule of collateral is not included, the lender must provide collateral and lienholder information to the Standard 7(a) Loan Guaranty Processing Center to complete the loan authorization.

⁵³ SBA, "SOP 50 10 5(H): Lender and Development Company Loan Programs," (effective May 1, 2015), p. 164, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

⁵⁴ *Ibid.*, p. 196.

⁵⁵ P.L. 93-386, the Small Business Amendments of 1974, provided the SBA authorization to charge fees to "cover administrative expenses and probable losses" on its loan guaranty programs.

⁵⁶ P.L. 108-447, the Consolidated Appropriations Act, 2005 (Division K—Small Business, Section 102. Loan Guaranty Fees) established the SBA's current maximum up-front guaranty fees as: up to 2% of the SBA guaranteed portion of 7(a) loans of \$150,000 or less, up to 3% of the SBA guaranteed portion of 7(a) loans exceeding \$150,000 but not more (continued...)

fee is a percentage of the SBA guaranteed portion of the loan. On short-term loans (maturities of less than 12 months), the lender must submit the guaranty fee to the SBA with the application for guaranty. The application will not be processed without the fee. On loans with maturities in excess of 12 months, the lender must pay the guaranty fee to the SBA within 90 days of the date of loan approval. Lenders 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 guaranty fee on loans with a gross amount of \$150,000 or less.⁵⁷

The annual service fee cannot exceed 0.55% of the outstanding balance of the SBA's share of the loan and is required to be no more than the "rate necessary to reduce to zero the cost to the Administration" of making guaranties.⁵⁸ The lender's annual service fee to the SBA cannot be charged to the borrower.⁵⁹

In FY2013, the SBA charged the maximum fees allowable. As shown in **Table 1**, the SBA has waived its annual service fee and up-front guaranty fee for all 7(a) loans of \$150,000 or less approved in FY2014 and FY2015. It has also reduced its annual service fee for all other 7(a) loans from 0.55% in FY2013 to 0.52% in FY2014 to 0.519% in FY2015.

Also, as mentioned previously, the SBA has waived its up-front, one-time loan guaranty fee for all veteran loans under the 7(a) SBAExpress program (up to \$350,000) from January 1, 2014, through the end of FY2015 and, in FY2015, for 50% of the up-front loan guaranty fee on all non-SBAExpress 7(a) loans (of \$150,001 up to and including \$5 million) for veterans.⁶⁰

(...continued)

than \$700,000, and up to 3.5% of the SBA guaranteed portion of 7(a) loans exceeding \$700,000. In addition, 7(a) loans with an SBA guaranteed portion in excess of \$1 million can be charged an additional 0.25% guaranty fee on the guaranteed amount in excess of \$1 million. See 15 U.S.C. §636(a)(18)(a); and SBA, "Small Business Jobs Act: Implementation of Conforming and Technical Amendments," 76 *Federal Register* 63544-63545, October 13, 2011.

⁵⁷ SBA, "SOP 50 10 5(H): Lender and Development Company Loan Programs," (effective May 1, 2015), p. 141, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf. The guaranty 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 electronically to <http://www.pay.gov> within 10 business days from the date the loan number is assigned and before the lender signs the Authorization for the SBA. For SBA Express and Export Express loans with a maturity of 12 months or less, the lender does not send the fee to the processing center with the request for loan number. The lender must pay the guaranty fee within 10 business days from the date the loan number is assigned and before the lender signs the Authorization for SBA.

⁵⁸ 15 U.S.C. §636(a)(23)(a).

⁵⁹ 15 U.S.C. §636(a)(23)(b).

⁶⁰ SBA, *FY2015 Congressional Budget Justification and FY2013 Annual Performance Report*, p. 10, at https://www.sba.gov/sites/default/files/files/FY15_CBJ_FY%202013_APR.pdf; and SBA, "SBA Will Continue to Zero Out Fees on Small Dollar Loans, Expands Relief for Larger Loans to Vets," October 1, 2014, at <https://www.sba.gov/content/sba-will-continue-zero-out-fees-small-dollar-loans-expands-relief-larger-loans-vets>.

Table I. SBA Annual Service and Guaranty Fees, FY2013-FY2015

Maturity and Gross Loan Amount	Annual Service Fee			Guaranty Fee		
	FY2013	FY2014	FY2015	FY2013	FY2014	FY2015
12 months or less and \$150,000 or less	0.55%	0.00%	0.00%	0.25%	0.00%	0.00%
12 months or less and more than \$150,000	0.55%	0.52%	0.519%	0.25%	0.25%	0.25%
Exceeding 12 months and \$150,000 or less	0.55%	0.00%	0.00%	2.00%	0.00%	0.00%
Exceeding 12 months and \$150,001 to \$700,000	0.55%	0.52%	0.519%	3.00%	3.00%	3.00% ^a
Exceeding 12 months and \$700,001 to \$5,000,000	0.55%	0.52%	0.519%	3.5% up to \$1 million +3.75% over \$1 million	3.5% up to \$1 million +3.75% over \$1 million	3.5% up to \$1 million +3.75% over \$1 million ^a

Source: U.S. Small Business Administration (SBA), “SBA Information Notice: 7(a) and 504 Fees Effective on October 1, 2013,” at <https://www.sba.gov/sites/default/files/5000-1288.pdf>; and U.S. Small Business Administration, “SBA Information Notice: 7(a) and 504 Fees Effective October 1, 2014,” at https://www.sba.gov/sites/default/files/lender_notices/5000-1318.pdf.

Notes: The annual service fee is a percentage of the outstanding balance of the SBA’s share of the loan. The guaranty fee is a percentage of the SBA guaranteed portion of the loan. If two or more SBA guaranteed loans are approved within 90 days of each other, the guaranty fee is determined based on the aggregate amount of the loans. Lenders are not permitted to split loans for the purpose of avoiding fees.

- a. In FY2015, the SBA is waiving 50% of the up-front loan guaranty fee on all non-SBAExpress 7(a) loans to veterans exceeding \$150,000 and the up-front, one-time loan guaranty fee for all veteran loans under the 7(a) SBAExpress program (up to \$350,000).

Because the guaranty fee for loans of \$150,000 or less is zero, lenders may not charge a guaranty fee for these loans to the borrower.⁶¹

The Obama Administration argued that the fee waivers for 7(a) loans of \$150,000 or less are necessary because the demand for smaller 7(a) loans had fallen and the waiver reduction “can be achieved with zero credit subsidy appropriations” because the “annual fees for larger 7(a) loans will cover the cost for those smaller loans.”⁶² The Administration also contended that waiving the fees on smaller SBA loans would “promote lending to small businesses that face the most constraints on credit access.”⁶³

For context, the SBA approved 34,282 7(a) loans of \$150,000 or less, totaling \$1.65 billion in FY2010 (13.1% of the total amount approved); 29,682 7(a) loans of \$150,000 or less, totaling \$1.63 billion in FY2011 (8.3% of the total amount approved); 25,486 7(a) loans of \$150,000 or

⁶¹ SBA, “SBA Information Notice: 7(a) and 504 Fees Effective on October 1, 2013,” at <https://www.sba.gov/sites/default/files/5000-1288.pdf>; and SBA, “SBA Information Notice: 7(a) and 504 Fees Effective October 1, 2014,” at https://www.sba.gov/sites/default/files/lender_notices/5000-1318.pdf.

⁶² SBA, *Fiscal Year 2014 Congressional Budget Justification and FY 2012 Annual Performance Report*, p. 36.

⁶³ U.S. Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2014: Small Business Administration*, p. 164, at <https://www.whitehouse.gov/sites/default/files/omb/budget/fy2014/assets/business.pdf>.

less, totaling \$1.43 billion in FY2012 (9.5% of the total amount approved); 24,923 7(a) loans of \$150,000 or less, totaling \$1.45 billion in FY2013 (8.1% of the total amount approved); and 30,675 7(a) loans of \$150,000 or less, totaling \$1.86 billion in FY2014 (9.7% of the total amount approved).⁶⁴

The SBA also announced that eliminating the annual service and guaranty fees for 7(a) loans of \$150,000 or less is part of its broader effort to “reduce barriers, attract new lenders, grow loan volumes of existing lenders and improve access to capital for small businesses and entrepreneurs.”⁶⁵

Some in Congress have questioned whether it is appropriate to require borrowers of larger 7(a) loans to, in effect, subsidize borrowers of smaller 7(a) loans, who might be direct competitors. They have suggested that it might be more appropriate to reduce fees across-the-board without regard to loan size.⁶⁶

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.⁶⁷

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 cannot 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.⁶⁸ 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.⁶⁹

⁶⁴ SBA, “SBA Lending Statistics for Major Programs (as of 9/30/2012),” at <https://www.sba.gov/sites/default/files/SBA%207a%20and%20504%20Gross%20Loan%20Approval%20Volume%20as%20of%209-30-2012.pdf>; SBA, “SBA Lending Statistics for Major Programs (as of 9/30/2013),” at <https://www.sba.gov/sites/default/files/SBA%207a%20and%20504%20Gross%20Loan%20Approval%20Volume%20as%2009-30-13.pdf>; and SBA, “SBA Lending Statistics for Major Programs (as of 9/30/2014),” at https://www.sba.gov/sites/default/files/aboutsbaarticle/WebsiteReport_asof9_30_2014.pdf.

⁶⁵ SBA, *FY 2014 Congressional Budget Justification and FY 2012 Annual Performance Report*, p. 4.

⁶⁶ For example, see Barry Pineles, Chief Counsel, House Committee on Small Business, “Hearing Memorandum on The Budget Outlook for Small Business Administration,” April 18, 2013, pp. 11-12, at http://smallbusiness.house.gov/uploadedfiles/revised_hearing_memo_4-24-2013.pdf.

⁶⁷ 13 C.F.R. §120.221.

⁶⁸ *Ibid.*; and SBA, “SOP 50 10 5(H): Lender and Development Company Loan Programs,” (effective May 1, 2015), pp. 145, 149, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

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

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.⁷⁰

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 1 year during the first 3 years after first disbursement. The fee is 5% of the prepayment amount during the first year, 3% in the second year, and 1% in the third year.⁷¹

Program Statistics

Loan Volume

The SBA generally uses the number and amount of loans approved each fiscal year, as opposed to the number and amount of loans disbursed, for making comparisons of lending volume among its loan guaranty programs. Although loan disbursement data can be useful, loan disbursements in one fiscal year typically include significant amounts approved in previous fiscal years. For example, in FY2012, 38% of 7(a) loan disbursements were from loans approved prior to FY2012.⁷²

The number of 7(a) loans approved annually is typically 10% to 20% higher than the number of loans disbursed (e.g., some borrowers decide not to accept the loan or there is a change in business ownership). The amount of 7(a) loans approved annually is typically 10% to 15% higher than the amount disbursed.

As shown in **Table 2**, the total number and amount of SBA 7(a) loans approved declined in FY2008 and FY2009, increased during FY2010 and FY2011, declined somewhat in FY2012, and increased in FY2013 and FY2014.

Table 2. 7(a) Loan Guaranty Program, Loan Volume, FY2007-FY2014

FY	Number of Loans Approved	Amount Approved (in billions)	Total Unpaid Principal Balance (in billions)
2007	99,606	\$14.3	\$46.1
2008	69,434	\$12.7	\$47.7
2009	41,289	\$9.2	\$48.6
2010	47,002	\$12.4	\$50.8

⁷⁰ 13 C.F.R. §120.221; and SBA, “SOP 50 10 5(H): Lender and Development Company Loan Programs,” (effective May 1, 2015), pp. 145, 149, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

⁷¹ 13 C.F.R. §120.223; and SBA, “SOP 50 10 5(H): Lender and Development Company Loan Programs,” (effective May 1, 2015), pp. 146, 150, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

⁷² SBA, Office of Congressional and Legislative Affairs, correspondence with the author, September 17, 2012. The SBA maintains selected disbursement data and will provide that data to congressional offices upon request.

FY	Number of Loans Approved	Amount Approved (in billions)	Total Unpaid Principal Balance (in billions)
2011	53,706	\$19.6	\$56.4
2012	44,377	\$15.2	\$60.1
2013	46,399	\$17.9	\$63.7
2014	52,044	\$19.2	\$68.2

Sources: SBA, *Agency Financial Report Fiscal Year 2010*, November 15, 2010, p. 7; SBA, *Fiscal Year 2011 Congressional Budget Justification and FY 2009 Annual Performance Report*, pp. 36, 125; SBA, “SBA Lending Statistics for Major Programs (as of 9/30/2012),” at <https://www.sba.gov/sites/default/files/aboutsbaarticle/SBA%207a%20and%20504%20Gross%20Loan%20Approval%20Volume%20as%20of%209-30-2012.pdf>; SBA, “SBA Lending Statistics for Major Programs (as of 9/30/2013),” at <https://www.sba.gov/sites/default/files/SBA%207a%20and%20504%20Gross%20Loan%20Approval%20Volume%20as%20of%209-30-13.pdf>; SBA, “SBA Lending Statistics for Major Programs (as of 9/30/2014),” at https://www.sba.gov/sites/default/files/aboutsbaarticle/WebsiteReport_asof9_30_2014.pdf; and SBA, “Table 1—Unpaid Principal Balance By Program,” at https://www.sba.gov/sites/default/files/files/WDS_Table1_UPB_Report.pdf.

Notes: The number of 7(a) loans approved annually is typically 10% to 20% higher than the number of loans disbursed (e.g., a borrower decides not to accept the loan or a change in business ownership). The amount of 7(a) loans approved annually is typically 10% to 15% higher than the amount disbursed. SBA, Office of Congressional and Legislative Affairs, correspondence with the author, November 21, 2013.

The SBA attributed the decreased number and amount of 7(a) loans approved in FY2008 and FY2009 to a reduction in the demand for small business loans resulting from the economic uncertainty of the recession (December 2007-June 2009) and to tightened loan standards imposed by lenders concerned about the possibility of higher loan default rates resulting from the economic slowdown. The SBA attributed the increased number of loans approved in FY2010 and FY2011 to legislation that provided funding to temporarily reduce the 7(a) program’s loan fees and temporarily increase the 7(a) program’s loan guaranty percentage to 90% for all standard 7(a) loans from up to 85% of loans of \$150,000 or less and up to 75% of loans exceeding \$150,000.⁷³ The fee subsidies and 90% loan guaranty percentage were in place during most of FY2010 and the first quarter of FY2011.⁷⁴ The increased number and amount of 7(a) loans approved in

⁷³ SBA, Press Office, “Recovery Loan Incentives Spurred Continued Rebound in SBA Lending in FY2010,” October 4, 2010, at <https://www.sba.gov/content/recovery-loan-incentives-spurred-continued-rebound-sba-lending-fy2010>; and SBA, “Jobs Act Supported More Than \$12 Billion in SBA Lending to Small Businesses in Just Three Months,” January 3, 2011, at <https://www.sba.gov/content/jobs-act-supported-more-12-billion-sba-lending-small-businesses-just-three-months>.

⁷⁴ P.L. 111-5, the American Recovery and Reinvestment Act of 2009 (ARRA), enacted on February 17, 2009, provided the SBA \$375 million to temporarily reduce fees in the 7(a) and 504/CDC loan guaranty programs, and increase the 7(a) program’s maximum loan guaranty percentage to 90% for all standard 7(a) loans through September 30, 2010, or until available funds were exhausted. Due to the increased demand for 7(a) loans, available funding was anticipated to be exhausted in early January 2010. 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. The fee subsidies and 90% loan guaranty percentage expired on May 31, 2010. P.L. 111-240, the Small Business Jobs Act of 2010, enacted on September 27, 2010, provided the SBA \$505 million (plus an additional \$5 million for related administrative expenses) to reinstate the fee subsidies and 90% maximum loan guaranty percentage through December 31, 2010, or until (continued...)

FY2013 and FY2014 compared with FY2012 are generally attributed to improving economic conditions.⁷⁵

Table 2 also provides, for comparison purposes, the total amount of the 7(a) program's unpaid principal balance by fiscal year. Precise measurements of the total credit market for small businesses are not available. However, the SBA has estimated that the credit market for small businesses (outstanding bank loans of \$1 million or less, plus credit extended by finance companies and other sources) is roughly \$1.0 trillion.⁷⁶ As of September 30, 2014, the SBA's 7(a) program's unpaid principal balance was \$68.2 billion, or about 6.7% of that amount.⁷⁷

Appropriations for Loan Subsidy Costs

One of the SBA's goals is to achieve a zero subsidy rate for its loan guaranty programs. A zero subsidy rate occurs when the SBA's loan guaranty programs generate sufficient revenue through fee collections and recoveries of collateral on purchased (defaulted) loans to not require appropriations to issue new loan guarantees. From 2005 to 2009, the SBA did not request appropriations to subsidize the cost of any of its loan guaranty programs, including the 7(a) program. However, as indicated in **Table 3**, loan guaranty fees and loan liquidation recoveries did not generate enough revenue to cover loan losses in the 7(a) loan guaranty program from FY2010 through FY2013 and in the 504/CDC loan guaranty program from FY2012 through FY2015. Appropriations were provided to address the shortfalls.

The Obama Administration indicated in its FY2016 budget request that the 7(a) and 504/CDC loan guaranty programs will not need appropriations for business loan credit subsidies in FY2016.⁷⁸

(...continued)

available funds were exhausted. 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.

⁷⁵ A small portion of the increase may also have been a result of an increase in 7(a) loan applications during the final two weeks of FY2013 as borrowers and lenders anticipated a possible federal government shutdown starting on October 1, 2013 (the first day of FY2014). See J.D. Harrison, "Shutdown yields slowdown: SBA returns to hundreds of small-business loans," *The Washington Post*, October 18, 2013. Prior to September 13, 2013, the SBA approved, on average, about 857 loans totaling \$320,787 per week during FY2013 (42,851 loan approvals totaling \$16,039,363 as of September 13, 2013, the 50th week of the fiscal year). The SBA approved 3,548 loans totaling \$1,828,918 during the final two weeks (and a day) of FY2013. See SBA, "SBA Lending Statistics for Major Programs (as of 9/13/2013, 9/20/2013, 9/27/2013, 9/30/2013, and 9/30/2014)," at <https://www.sba.gov/about-sba/sba-newsroom/weekly-lending-report>. The federal government shutdown subsequently occurred on October 1, 2013, and continued through October 16, 2013.

⁷⁶ SBA, Office of Advocacy, "Frequently Asked Questions About Small Business Finance," February 2014, at https://www.sba.gov/sites/default/files/2014_Finance_FAQ.pdf.

⁷⁷ SBA, "Table 1 — Unpaid Principal Balance By Program," at https://www.sba.gov/sites/default/files/files/WDS_Table1_UPB_Report.pdf.

⁷⁸ SBA, *FY 2016 Congressional Budget Justification and FY 2014 Annual Performance Report*, p. 16.

Table 3. Business Loan Credit Subsidies, 7(a) and 504/CDC Loan Guaranty Programs, FY2007-FY2016

(\$ in millions)

FY	7(a)	504/CDC	Total Subsidy
2007	\$0.0	\$0.0	\$0.0
2008	\$0.0	\$0.0	\$0.0
2009	\$0.0	\$0.0	\$0.0
2010	\$80.0	\$0.0	\$80.0
2011	\$80.0	\$0.0	\$80.0
2012	\$139.4	\$67.7	\$207.1
2013	\$213.8	\$102.5	\$316.3
2014	\$0.0	\$107.0	\$107.0
2015	\$0.0	\$45.0	\$45.0
2016 request	\$0.0	\$0.0	\$0.0

Source: SBA, FY2011 Congressional Budget Justification and FY2009 Annual Performance Report, p. 19; SBA, FY2012 Congressional Budget Justification and FY2010 Annual Performance Report, p. 22; SBA, FY2013 Congressional Budget Justification and FY2011 Annual Performance Report, p. 19; SBA, FY2014 Congressional Budget Justification and FY2012 Annual Performance Report, p. 25; SBA, FY2015 Congressional Budget Justification and FY2013 Annual Performance Report, p. 24; P.L. 113-235, the Consolidation and Further Continuing Appropriations Act, 2015; and SBA, FY2016 Congressional Budget Justification and FY2014 Annual Performance Report, p. 16.

Notes: The Microloan program also receives a credit subsidy, primarily for providing below market interest rates to Microloan intermediaries. The subsidies were \$1.3 million in FY2007, \$2.0 million in FY2008, \$2.5 million in FY2009, \$3.0 million in FY2010 and FY2011, \$3.678 million in FY2012, \$3.498 million (after sequestration) in FY2013, \$4.6 million in FY2014, and \$2.5 million in FY2015. The Obama Administration has requested \$3.338 million for Microloan credit subsidies for FY2016.

Administrative Expenses

In FY2014, the SBA spent \$66.5 million on the 7(a) program for administrative expenses, including \$40.6 million for loan making, \$5.8 million for loan servicing, and \$20.1 million for loan liquidation. Also, the SBA spent \$27.0 million on lender oversight, including oversight of 7(a) lenders. The SBA anticipates that 7(a) program administrative expenses will be about \$65.9 million in FY2015, and that it will spend about \$27.1 million on lender oversight for the SBA's various lending programs.⁷⁹

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

⁷⁹ Ibid., p. 26.

- 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%);
- hire additional staff (6%);
- build new building (4%);
- purchase new land (3%); and
- improve land (2%).⁸⁰

The Urban Institute also reported that most of the 7(a) borrowers responding to the 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).⁸¹ 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).⁸²

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.⁸³ In FY2014, 28.9% of 7(a) loan approvals (\$5.54 billion of \$19.19 billion) were to minority-owned businesses (21.3% Asian, 5.3% Hispanic, 1.8% African-American, 0.5% American Indian, and 0.01% multi-group) and 13.3% were to women-owned businesses.⁸⁴ From its comparative analysis of conventional small business loans and the SBA's loan guaranty programs, the Urban Institute concluded:

⁸⁰ Christopher Hayes, *An Assessment of Small Business Administration Loan and Investment Performance: Survey of Assisted Businesses* (Washington, DC: The Urban Institute, 2008), p. 3, at 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.

⁸¹ *Ibid.*, p. 5.

⁸² *Ibid.*

⁸³ 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, at http://www.urban.org/UploadedPDF/411596_504_gap_analysis.pdf.

⁸⁴ SBA, "SBA Lending Statistics for Major Programs (as of 9/30/2014)," at https://www.sba.gov/sites/default/files/aboutsbaarticle/WebsiteReport_asof9_30_2014.pdf.

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.⁸⁵

Congressional Issues

Access to Capital

Congressional interest in the 7(a) loan program has increased in recent years largely because of concerns that small businesses might be prevented from accessing sufficient capital to enable them to assist in the economic recovery. During the 110th and 111th Congresses, several laws were enacted to increase the supply and demand for capital for both large and small businesses.⁸⁶ 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."⁸⁷ 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.⁸⁸

⁸⁵ 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. 21, at http://www.urban.org/UploadedPDF/411596_504_gap_analysis.pdf.

⁸⁶ For further analysis, see CRS Report R40985, *Small Business: Access to Capital and Job Creation*, by Robert Jay Dilger.

⁸⁷ P.L. 110-343, the Emergency Economic Stabilization Act of 2008.

⁸⁸ U.S. Department of the Treasury, *Troubled Assets Relief Program Monthly 105(a) Report—November 2010*, December 10, 2010, pp. 2-4, at [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," March 16, 2009, at https://www.whitehouse.gov/the_press_office/Remarks-by-the-President-to-small-business-owners/.

In addition, 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 \$505 million (plus \$5 million for administrative expenses) 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, or until the available funding was exhausted.⁸⁹ Funding for these purposes was 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."⁹⁰ 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.⁹¹

Program Administration

Over the years, 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 SBA's loan guaranty programs. Although improvements have been noted, 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

On December 1, 2000, the OIG released its FY2001 list of the most serious management challenges facing the SBA and included, for the first time, the oversight of SBA lenders.⁹² Since then, the OIG has determined that the SBA has made significant progress in improving its

⁸⁹ P.L. 111-240, the Small Business Jobs Act of 2010, §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.

⁹⁰ SBA, "Administration Announces New Small Business Commercial Real Estate and Working Capital Programs," February 5, 2010, at <http://www.illinois.gov/dceo/SmallBizAssistance/CenterConnect/WeeklyConnect/SBA%20Fact%20Sheet%20CRE%20REFI%20and%20WORKING%20CAPITAL.docx>.

⁹¹ Susan Eckerly, "NFIB Responds to President's Small Business Lending Initiatives," Washington, DC, October 21, 2009, at <http://www.nfib.com/newsroom/newsroom-item/cmsid/50080/>; and NFIB, "Government Spending," Washington, DC, at <http://www.nfib.com/issues-elections/issues-elections-item/cmsid/49051/>.

⁹² SBA, Office of Inspector General, "FY2001 Agency Management Challenges," December 1, 2000, pp. 15-17.

oversight of SBA lenders. For example, the OIG commended the SBA for (1) developing risk profiles and lender performance thresholds, (2) creating a Select Analytical Review process to allow for virtual risk-based reviews, (3) updating its lender risk rating model to better stratify and predict risk, and (4) conducting test reviews under the new risk-based review protocol. However, the OIG continues to list lender oversight as one of the most serious management challenges facing the SBA because it argues that several issues have not been fully addressed. Specifically, the OIG reports that the SBA needs to “implement and demonstrate the effectiveness of the process for monitoring and verifying lenders’ implementation of corrective actions.”⁹³

The Need for an Agency-Wide Quality Control Program

In 2000, the OIG noted that “private lenders are performing an increasing percentage of loan underwriting, servicing, and liquidation functions that were previously performed by SBA staff” and that a summary audit of the 7(a) loan program in 1999 which it had conducted found that “lenders did not consistently comply with 22 key processing procedures.”⁹⁴ The OIG also noted that GAO had found in 1998 “that in the five district offices visited, SBA had not performed an on-site visit review of about 96% of the lenders in the past 5 years.”⁹⁵

In response to these concerns, the SBA established an Office of Lender Oversight (renamed the Office of Credit Risk Management in 2007), led by an Associate Administrator. In October 2000, that office drafted a strategic plan to serve as a basis for developing a Standard Operating Procedure (SOP) for lender oversight and, among other activities, initiated “steps to develop and implement a comprehensive loan monitoring system to evaluate lender performance. The system will collect data on lenders such as delinquency default rates, liquidations, loan payments, and loan originations.”⁹⁶

Over the next several years, the SBA took a number of actions to improve its oversight of 7(a) lenders. For example, in 2004, the SBA’s National Guaranty Purchase Center developed a quality control plan “to review the quality of the guaranty purchase process.”⁹⁷ In 2006, the SBA issued an SOP that established procedures for on-site, risk-based lender reviews and safety and soundness examinations for 7(a) lenders and Certified Development Companies (CDCs) participating in the SBA’s 504/CDC loan guaranty program.⁹⁸ In 2007, the SBA completed the centralization of all 7(a) loan processing activities and, with very limited exception, ended loan making, servicing, liquidation, and guaranty purchase activity at district offices.⁹⁹ In 2008, the

⁹³ SBA, Office of Inspector General, “Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration In Fiscal Year 2014,” October 31, 2013, at <https://www.sba.gov/sites/default/files/%5Bc%5DFY%202014%20Management%20Challenges%20OIG%20Report%2014-01.pdf>.

⁹⁴ SBA, Office of Inspector General, “FY2001 Agency Management Challenges,” December 1, 2000, p. 15.

⁹⁵ Ibid.

⁹⁶ Ibid., p. 17.

⁹⁷ SBA, Office of Inspector General, “Improvement is Needed to Ensure Effective Quality Control at Loan Operation Centers,” January 17, 2014, p. 1, at <https://www.sba.gov/sites/default/files/Audit%20Evaluation%20Report%2014-08%20Improvement%20is%20Needed%20to%20Ensure%20Effective%20Quality%20Control%20at%20Loan%20Operation%20Centers.pdf>.

⁹⁸ SBA, Office of Lender Oversight, “SOP 51-00: On-Site Lender Reviews/Examinations,” (effective September 28, 2006), at https://www.sba.gov/sites/default/files/sop_51-00-pdf.pdf. Note: Although on-site reviews are generally conducted on all 7(a) lenders with outstanding balances on the SBA-guaranteed portions of its loan portfolio amounting to \$10 million or more, the SBA may conduct on-site reviews of any SBA lender, as it considers necessary.

⁹⁹ SBA, *FY 2009 Congressional Budget Justification and FY 2007 Annual Performance Report*, p. 37.

SBA issued an SOP for 7(a) lender oversight which included uniform policies and procedures for the evaluation of lender performance.¹⁰⁰ In October 2008, the SBA's Office of Financial Program Operations (OFPO) began designing "a comprehensive quality control program across all of its centers."¹⁰¹ Previously, quality control was conducted within each loan center (Standard 7(a) Loan Guaranty Processing Center, Commercial Loan Service Center, and National Guaranty Purchase Center) "at various levels of sophistication."¹⁰² The SBA also issued an interim final rule in the *Federal Register* on December 1, 2008, incorporating the SBA's risk-based lender oversight program into the SBA's regulations.¹⁰³

Nonetheless, in 2009, the OIG argued that the 7(a) loan guaranty program continued to be "vulnerable to fraud and unnecessary losses because [the SBA] 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.¹⁰⁴

The OIG noted at that time that its review of the 7(a) program's FY2008 lending 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 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, 2008.¹⁰⁵ In addition, the OIG's review of a sample of 30 7(a) loans issued in FY2008 found 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.¹⁰⁶ The OIG concluded that the SBA needed to strengthen its oversight of 7(a) lenders to "establish more robust controls to prevent waste, fraud, abuse, and inefficiencies."¹⁰⁷

In 2009, GAO also recommended that the SBA strengthen its oversight of 7(a) 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."¹⁰⁸ It also noted that

¹⁰⁰ SBA, Office of Financial Assistance, "SOP 50-10(5): Lender and Development Company Loan Programs," (effective August 1, 2008), at https://www.sba.gov/sites/default/files/sop_51-00-pdf.pdf.

¹⁰¹ SBA, Office of Inspector General, "Improvement is Needed to Ensure Effective Quality Control at Loan Operation Centers," January 17, 2014, p. 15, at <https://www.sba.gov/sites/default/files/Audit%20Evaluation%20Report%2014-08%20Improvement%20is%20Needed%20to%20Ensure%20Effective%20Quality%20Control%20at%20Loan%20Operation%20Centers.pdf>.

¹⁰² Ibid. The Standard 7(a) Loan Guaranty Processing Center, located in Citrus Heights, CA and Hazard, KY, processes 7(a) loan guaranty applications and conducts limiting servicing of 7(a) loans. The Commercial Loan Service Center, located in Fresno, CA and Little Rock, AR, is responsible for loan servicing actions (after loans are disbursed), SBAExpress loan purchases, and 504/CDC loan guaranty program liquidation. The National Guaranty Purchase Center, located in Herndon, VA, processes 7(a) guaranty purchase requests and conducts liquidation oversight.

¹⁰³ SBA, "Lender Oversight Program," 73 *Federal Register* 75498-75527, December 11, 2008.

¹⁰⁴ SBA, Office of Inspector General, "Semiannual Report to Congress, Fall 2009," p. 5, at https://www.sba.gov/sites/default/files/oig/oig_fall2009sar.pdf.

¹⁰⁵ Ibid., p. 5.

¹⁰⁶ Ibid.

¹⁰⁷ Ibid., p. 3.

¹⁰⁸ GAO, *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, at <http://www.gao.gov/new.items/d1053.pdf>.

the SBA targets for review those lenders with the largest SBA-guaranteed loan portfolios. As a result of this approach, 97% 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.¹⁰⁹

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."¹¹⁰

Agency-Wide Quality Control Program Implementation

In 2010, the SBA's OFPO established its agency-wide quality control program, which is designed to improve service and "reduce waste, fraud, and abuse" by ensuring "that centers accurately and consistently apply statutory, regulatory, and procedural loan program requirements."¹¹¹ The quality control program is led in each center by a designated quality control specialist. Each center is tasked with establishing specific quality review activities and targets, and creating a center specific quality program guide to detail (1) the center's activities that require quality reviews, (2) the number of reviews required (daily or monthly) by type of transaction, (3) compliance goals, and (4) the required corrective action activities.¹¹²

Also in 2010, the SBA noted that it had developed a "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."¹¹³ 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.¹¹⁴

The SBA asserted 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

¹⁰⁹ Ibid., pp. i, 27-30.

¹¹⁰ Ibid., p. 35. 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." See GAO, *Small Business Administration: Additional Guidance on Documenting Credit Elsewhere Decisions Could Improve 7(a) Program Oversight*, GAO-09-228, February 12, 2009, p. 3, at <http://www.gao.gov/new.items/d09228.pdf>.

¹¹¹ SBA, Office of Inspector General, "Improvement is Needed to Ensure Effective Quality Control at Loan Operation Centers," January 17, 2014, p. 3, at <https://www.sba.gov/sites/default/files/Audit%20Evaluation%20Report%2014-08%20Improvement%20is%20Needed%20to%20Ensure%20Effective%20Quality%20Control%20at%20Loan%20Operation%20Centers.pdf>.

¹¹² Ibid., pp. 6, 16.

¹¹³ SBA, *Fiscal Year 2011 Congressional Budget Justification and FY 2009 Annual Performance Report*, p. 6.

¹¹⁴ Ibid., p. 43.

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.¹¹⁵

In January 2014, the OIG released an evaluation of the SBA's agency-wide quality control program. The OIG's evaluation was conducted from March 2013 through September 2013. The OIG concluded that the SBA had "made significant progress" in implementing a quality control program for its loan centers, but also found that "quality control activities were not being performed at the centers in accordance with SBA's overall Quality Control and Assurance Program Guide and Center specific guidance."¹¹⁶ The OIG noted that the loan centers omitted required quality control reviews of significant functions, discontinued regularly scheduled quality reviews for about five months during FY2012 to focus on reviews required by the Improper Payments Elimination and Recovery Act of 2010, and did not appropriately track corrective actions until resolution on deficiencies identified by center quality control teams.¹¹⁷

The OIG recommended that the SBA (1) ensure the proper allocation of resources and scoping of the quality control program to complete required quality control activities at the loan operations centers; (2) ensure that corrective actions related to quality control findings are appropriately documented and completed within required timeframes; and (3) establish and implement a plan to conduct quality assurance activities at SBA loan operation centers.¹¹⁸

The SBA agreed with the OIG's recommendations and indicated that it was taking action to address them. For example, the SBA indicated that the OFPO had already "hired quality control specialists and initiated a process improvement project dedicated to ensure adequate staffing is available";¹¹⁹ and had "initiated a project to redevelop the corrective action process, which resulted in the development and implementation of the Corrective Action Tracker [started in October 2013 and fully operational in January 2014]," which "maintains and provides consistent data for tracking and analyzing loan-level deficiencies status and trends across centers."¹²⁰ The SBA also indicated that it was reviewing the existing quality program guides for each center and will establish an initial quality assurance plan by March 30, 2014.¹²¹

In June 2014, the OIG released an evaluation of the SBA's management of the 7(a) loan guaranty approval process. From June 2013 through March 2014, the OIG reviewed 70 loans approved by

¹¹⁵ Ibid.

¹¹⁶ SBA, Office of Inspector General, "Improvement is Needed to Ensure Effective Quality Control at Loan Operation Centers," January 17, 2014, p. 4, at <https://www.sba.gov/sites/default/files/Audit%20Evaluation%20Report%2014-08%20Improvement%20is%20Needed%20to%20Ensure%20Effective%20Quality%20Control%20at%20Loan%20Operation%20Centers.pdf>.

¹¹⁷ Ibid., pp. 4, 5.

¹¹⁸ Ibid., pp. 17-19.

¹¹⁹ Ibid., p. 11.

¹²⁰ Ibid., p. 17.

¹²¹ As of the publication date of this report, the SBA has not made any announcements concerning the establishment of this quality assurance plan.

the SBA's Loan Guaranty Processing Center (LGPC) during the period of April 1, 2011, to April 30, 2013, "to assess compliance with SBA's regulations and procedures."¹²² These loans totaled \$58 million. The OIG found that

based on a small judgmental sample of 13 loans approved for \$13 million, we identified that 11 loans approved for \$11.3 million had material underwriting deficiencies. Additionally, 6 of the 11 loans defaulted and the SBA purchased the guaranties for \$4.8 million, resulting in unnecessary losses. Further we conducted limited reviews of another 57 SBA-approved 7(a) loans that were transferred to liquidation and defaulted early. We found evidence that eight of these loans totaling \$5.6 million should not have been approved due to repayment ability and eligibility deficiencies.¹²³

The OIG concluded that

- LGPC management emphasized quantity over quality for 7(a) loan reviews;
- LGPC loan specialists were not provided adequate guidance and training to conduct their 7(a) loan review activities; and
- a decrease in the number of staff assigned to loan reviews, increase in loan size and complexity, additional LGPC responsibilities, and inadequate supervision also contributed to inappropriate loan decisions.¹²⁴

The OIG recommended that the SBA (1) revise its management reports to measure quality against established targets and ensure that production credit is given for all loan reviews; (2) distribute the LGPC Strategic Plan to staff and establish a process to ensure that quality goals are regularly communicated to LGPC staff; (3) develop and issue appropriate guidance that will assist loan specialists with their duties; (4) develop and implement a training plan and tracking system that ensures loan specialists develop and retain the required skills necessary to achieve organizational goals; and (5) allocate LGPC resources to ensure risk is mitigated and quality is emphasized in accordance with the LGPC Strategic Plan.¹²⁵

The SBA concurred with these recommendations and indicated that it was in the process of taking action to address them. For example, the OFPO indicated that it was revising its management reports to measure quality against established targets, continuing to distribute the LGPC Strategic Plan with an increased emphasis on the communication of quality goals, and inventorying existing guidance in an attempt to create a comprehensive manual for all LGPC staff that will be linked to all staff member's desktop computers.¹²⁶

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:

¹²² SBA, "Significant Opportunities Exist to Improve the Management of the 7(a) loan Guaranty Approval Process," June 6, 2014, p. 2, at <https://www.sba.gov/sites/default/files/%5Bc%5D%20Audit%20Report%2014-13.pdf>.

¹²³ *Ibid.*, p. 8.

¹²⁴ *Ibid.*

¹²⁵ *Ibid.*, p. 21.

¹²⁶ *Ibid.*, pp. 24-25.

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.¹²⁷

The SBA's 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 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 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."¹²⁸ 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.¹²⁹ 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."¹³⁰

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."¹³¹ In response to the OIG's recommendation to develop additional performance metrics for the Microloan program, the SBA reported that it had "contracted with the Aspen Institute to advise on appropriate program and performance metrics for both microloans and technical assistance grants."¹³² 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.

¹²⁷ GAO, *Small Business Administration: 7(a) Loan Program Needs Additional Performance Measures*, GAO-08-226T, November 1, 2007, p. 2, at <http://www.gao.gov/new.items/d08226t.pdf>.

¹²⁸ SBA, Office of the Inspector General, *SBA's Administration of the Microloan Program under the Recovery Act*, December 28, 2009, p. 6, at <https://www.sba.gov/sites/default/files/om10-10.pdf>.

¹²⁹ *Ibid.*

¹³⁰ *Ibid.*, p. 7.

¹³¹ GAO, *Small Business Administration: 7(a) Loan Program Needs Additional Performance Measures*, GAO-08-226T, November 1, 2007, p. 8, at <http://www.gao.gov/new.items/d08226t.pdf>.

¹³² SBA, Office of the Inspector General, *SBA's Administration of the Microloan Program under the Recovery Act*, December 28, 2009, p. 9, at <https://www.sba.gov/sites/default/files/om10-10.pdf>.

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. Congress did not approve any changes to the 7(a) program during the 112th Congress and has not approved any changes to the 7(a) program, to date, during the 113th 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%. Congress subsequently provided nearly \$1.1 billion to temporarily 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
- temporarily allow in FY2010 and FY2011, with an option to extend into FY2012, the refinancing of loans for owner-occupied commercial real estate that are within one year of maturity under the SBA's 504/CDC program.¹³³

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 would “allow the SBA to help America's small businesses drive long-term economic growth and the creation of jobs in communities across the country.”¹³⁴ The

¹³³ SBA, “Administration Announces New Small Business Commercial Real Estate and Working Capital Programs,” February 5, 2010, at <http://www.illinois.gov/dceo/SmallBizAssistance/CenterConnect/WeeklyConnect/SBA%20Fact%20Sheet%20CRE%20REFI%20and%20WORKING%20CAPITAL.docx>.

¹³⁴ Ibid.

Administration also argued that increasing the maximum loan limits for these programs would be “budget neutral” over the long run and “help improve the availability of smaller loans.”¹³⁵

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 higher loan limits 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.¹³⁶ 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.”¹³⁷

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.¹³⁸ 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 businesses’ access to capital. They argued that the best means to assist small business economic growth and job creation is to focus on small business tax reduction, reform of financial credit market regulation, and federal fiscal restraint.¹³⁹

P.L. 111-5, the American Recovery and Reinvestment Act of 2009 (ARRA)

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 (\$299 million) 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 (\$76 million).¹⁴⁰

¹³⁵ Ibid.

¹³⁶ Robb Mandelbaum, “Small Business Incentives Face a Hard Road in Congress,” *New York Times*, February 12, 2010, at <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.

¹³⁷ 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.

¹³⁸ Robb Mandelbaum, “Why Won’t the S.B.A. Lend Directly to Small Businesses?” *New York Times*, March 10, 2010, at <http://boss.blogs.nytimes.com/2010/03/10/why-wont-the-s-b-a-loan-directly-to-small-businesses/>.

¹³⁹ Susan Eckerly, “NFIB Responds to President’s Small Business Lending Initiatives,” Washington, DC, October 21, 2009, at <http://www.nfib.com/newsroom/newsroom-item/cmsid/50080/>; and NFIB, “Government Spending,” Washington, DC, at <http://www.nfib.com/issues-elections/issues-elections-item/cmsid/49051/>.

¹⁴⁰ SBA, “Recovery Act Agency Plan,” May 15, 2009, at https://www.sba.gov/sites/default/files/recovery_act_reports/sba_recovery_act_plan.pdf.

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

P.L. 111-240 provided \$505 million (plus \$5 million for administrative expenses) 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 available funding was exhausted (which occurred on January 3, 2011). The act also made the following changes to the SBA's programs:

- increased the maximum loan size for 7(a) loans from \$2 million to \$5 million;
- temporarily increased for one year (through September 27, 2011) the cap on SBAExpress loans from \$350,000 to \$1 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;
- 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 \$7.5 billion in short-term commercial real estate debt each fiscal year for two years after enactment (through September 27, 2012) into long-term fixed rate loans.¹⁴¹

The act also authorized 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.¹⁴² It also contained revenue raising provisions to offset the act's cost and authorized a number of changes to other SBA loan and contracting programs.

¹⁴¹ P.L. 111-240, the Small Business Jobs Act of 2010, Section 1122. Low-Interest Refinancing Under the Local Development Business Loan Program.

¹⁴² 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. For further analysis of the State Small Business Credit Initiative, see CRS Report R42581, *State Small Business Credit Initiative: Implementation and Funding Issues*, by Robert Jay Dilger.

Legislative Activity During the 112th Congress

As mentioned previously, Congress did not approve any changes to the 7(a) program during the 112th Congress. However, several bills were introduced during the 112th Congress that would have changed the program.

S. 1828, a bill to increase small business lending, and for other purposes, was introduced on November 8, 2011, and referred to the Senate Committee on Small Business and Entrepreneurship. The bill would have reinstated for a year following the date of its enactment the temporary fee subsidies for the 7(a) and 504/CDC loan guaranty programs and the 90% loan guaranty for standard 7(a) loans, which were originally authorized by ARRA and later extended by several laws, including the Small Business Jobs Act of 2010.

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 have extended 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 27, 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 have provided statutory authorization for the Patriot Express Pilot Program. This program was subsequently discontinued by the SBA on December 31, 2013. The bill would have increased the program's maximum loan amount from \$500,000 to \$1 million, and it would have increased the guaranty percentages 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.

Legislative Activity During the 113th Congress

H.R. 2451, the Strengthening Entrepreneurs' Economic Development Act of 2013, was introduced on June 20, 2013, and referred to the House Committee on Small Business. It would have authorized the SBA to make direct loans of up to \$150,000 to businesses with fewer than 20 employees. It would have also required the SBA to assess, collect, and retain a fee with respect to the outstanding balance of the deferred participation share of each 7(a) loan in excess of \$2 million that is no more than is necessary to reduce to zero the SBA's cost of making the loan.

H.R. 2461, the SBA Loan Paperwork Reduction Act of 2013, was introduced on June 20, 2013, and referred to the House Committee on Small Business. It would have provided statutory authorization for the Small Loan Advantage (SLA) pilot program. The SBA started that program on February 15, 2011. It provided a streamlined application process for 7(a) loans of up to \$350,000 if the loan received an acceptable credit score from the SBA prior to the loan being submitted for processing. The SBA adopted the SLA application process as the model for processing all non-express 7(a) loans of \$350,000 or less, effective January 1, 2014.

As mentioned previously, the Obama Administration has waived the up-front loan guaranty fee and ongoing servicing fee for 7(a) loans of \$150,000 or less approved in FY2014 and FY2015. H.R. 2462, the Small Business Opportunity Acceleration Act of 2013, introduced on June 20,

2013, and referred to the House Committee on Small Business, would have made this fee waiver permanent.

Also, the Obama Administration is waiving the up-front, one-time loan guaranty fee for veteran loans under the SBAExpress program (up to \$350,000) from January 1, 2014, through the end of FY2015 (called the Veterans Advantage Program). S. 2143, the Veterans Entrepreneurship Act, would have authorized this fee waiver and made it permanent. Also, P.L. 113-235 provided statutory authorization to waive the 7(a) SBAExpress program's guarantee fee for veterans (and their spouses) in FY2015.

Legislative Activity During the 114th Congress

As mentioned previously, S. 957, the Veterans Entrepreneurship Act, introduced on April 15, 2015, and reported favorably by the Senate Committee on Small Business and Entrepreneurship on June 10, 2015, would authorize and make permanent the up-front, one-time loan guaranty fee for veteran loans under the SBAExpress program. In addition, H.R. 2499, the Veterans Entrepreneurship Act of 2015, introduced on May 21, 2015, and reported favorably by the House Committee on Small Business on June 10, 2015, would authorize this fee waiver and make it permanent, subject to the 7(a) loan guaranty program, in its entirety, not having a subsidy cost.¹⁴³

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 businesses' access to capital and result in job retention and creation. As a general proposition, some, including President Obama, argued that the SBA should 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 create jobs.¹⁴⁴ 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 help small businesses further economic growth and job creation.¹⁴⁵

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

¹⁴³ U.S. Congress, House Committee on Small Business, *Veterans Entrepreneurship Act of 2015*, report to accompany H.R. 2499, 114th Cong., 1st sess., June 25, 2015, H.Rept. 114-187 (Washington: GPO, 2015), p. 9.

¹⁴⁴ 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, at <http://www.whitehouse.gov/the-press-office/remarks-president-job-creation-and-economic-growth>.

¹⁴⁵ Susan Eckerly, "NFIB Responds to President's Small Business Lending Initiatives," Washington, DC, October 21, 2009, at <http://www.nfib.com/newsroom/newsroom-item/cmsid/50080/>; and NFIB, "Government Spending," Washington, DC, at <http://www.nfib.com/issues-elections/issues-elections-item/cmsid/49051/>.

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 task. For example, a 2008 Urban Institute study concluded that differences in the term, interest rate, and amount of SBA financing were “not significantly associated with increasing sales or employment among firms receiving SBA financing.”¹⁴⁶ The study also reported that the 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.”¹⁴⁷

As the Urban Institute study suggests, because many factors influence business success, measuring the 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.¹⁴⁸ Other performance-oriented measures that Congress might also consider during the 114th Congress 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.

¹⁴⁶ 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, at http://www.urban.org/UploadedPDF/411602_executive_summary.pdf.

¹⁴⁷ *Ibid.*

¹⁴⁸ GAO, *Small Business Administration: 7(a) Loan Program Needs Additional Performance Measures*, GAO-08-226T, November 1, 2007, p. 2, at <http://www.gao.gov/new.items/d08226t.pdf>; and SBA, Office of the Inspector General, *SBA’s Administration of the Microloan Program under the Recovery Act*, December 28, 2009, pp. 6-7, at <https://www.sba.gov/sites/default/files/om10-10.pdf>.

Appendix. 7(a) Specialized Programs

The 7(a) program has several specialized programs that offer streamlined and expedited loan procedures for particular groups of borrowers, including the SBAExpress, Export Express, 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).¹⁴⁹ The program is 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.¹⁵⁰ It provides a 50% loan guaranty on loan amounts up to \$350,000.

In FY2014, the SBA approved 26,545 SBAExpress loans (51.0% of total 7(a) program loan approvals), totaling \$1.91 billion (9.9% of total 7(a) program amount approvals).¹⁵¹ The SBA approved 26,844 SBAExpress loans, totaling \$2.87 billion in FY2011; 23,149 SBAExpress loans, totaling \$1.78 billion in FY2012; and 21,761 SBAExpress loans, totaling \$1.68 billion in FY2013.¹⁵² The program's higher loan volume in FY2011 was due, at least in part, to a provision in 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 27, 2011).

During the 112th Congress, H.R. 2936, the Small Business Administration Express Loan Extension Act of 2011, would have extended the SBAExpress program's higher loan limit for an additional year (through September 27, 2012).

SBAExpress loan proceeds can be used for the same purposes as those of 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 that 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 those of the 7(a) program (the loan maturity for working capital, machinery, and equipment (not to exceed the life of the equipment) is typically 5 years to 10 years; and the loan

¹⁴⁹ The SBAExpress program was initially called FASTRAK and offered a 50% loan guaranty on loans of up to \$100,000. FASTRAK's program guidance was issued on March 6, 1995. See SBA, "FASTRAK," 60 *Federal Register* 12271-12275, March 6, 1995. A brief history of the SBAExpress program is provided in SBA, "SBAExpress Program Guide," (effective October 1, 2002), p. 3, at https://www.sba.gov/sites/default/files/files/sba_elending_clc_sbaexpress.pdf.

¹⁵⁰ SBA, "The SBA Express Pilot Program: Inspection Report," June 1998, p. 3.

¹⁵¹ SBA, "SBA Lending Statistics for Major Programs (as of 9/30/2014)," at https://www.sba.gov/sites/default/files/aboutsbaarticle/WebsiteReport_asof9_30_2014.pdf.

¹⁵² SBA, "SBA Lending Statistics for Major Programs (as of 9/30/2013)," at <https://www.sba.gov/sites/default/files/SBA%207a%20and%20504%20Gross%20Loan%20Approval%20Volume%20as%2009-30-13.pdf>; and SBA, "SBA Lending Statistics for Major Programs (as of 9/30/2014)," at https://www.sba.gov/sites/default/files/aboutsbaarticle/WebsiteReport_asof9_30_2014.pdf.

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 \$50,000.¹⁵³ The program has the same fees as those used in the 7(a) program. To account for the program's lower guaranty rate of 50%, lenders are allowed to perform their own loan analysis and procedures and receive SBA approval with a targeted 36-hour maximum turnaround time.¹⁵⁴ 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.

The SBA has waived the up-front, one-time loan guaranty fee for veteran loans under the SBAExpress program (up to \$350,000) from January 1, 2014, through the end of FY2015 (called the Veterans Advantage Program). The SBA announced that the fee waiver was part "of SBA's broader efforts to make sure that veterans have the tools they need to start and grow a business."¹⁵⁵

As mentioned previously, the SBA is also waiving the up-front loan guaranty fee and ongoing servicing fee for 7(a) loans of \$150,000 or less and 50% of the up-front loan guaranty fee on all non-SBAExpress 7(a) loans to veterans exceeding \$150,000 in FY2015.

In a related development, the SBA discontinued the Patriot Express Pilot Program on December 31, 2013. It provided loans of up to \$500,000 (with a guaranty of up to 85% of loans of \$150,000 or less and up to 75% of loans exceeding \$150,000) to veterans and their spouses.¹⁵⁶ It had been in operation since 2007, and, like the SBAExpress program, featured streamlined documentation requirements and expedited loan processing. Over its history, the Patriot Express Pilot Program disbursed 9,414 loans amounting to over \$791 million.¹⁵⁷

Export Express

The Export Express program was initially established as a subprogram of the SBAExpress program in 1998, and made a separate pilot program in 2000.¹⁵⁸ It was made permanent through

¹⁵³ SBA, "SBAExpress," at <https://www.sba.gov/content/sba-express>.

¹⁵⁴ Ibid.

¹⁵⁵ SBA, "SBA Announces New Measures to Help Get Small Business Loans Into the Hands of Veterans," November 8, 2013, at <https://www.sba.gov/content/sba-announces-new-measures-help-get-small-business-loans-hands-veterans>.

¹⁵⁶ Eligible businesses were required to 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 servicemember who died while in service, or a widowed spouse of a veteran who died of a service-connected disability. See SBA, "SOP 50 10 5(E): Lender and Development Company Loan Programs," (effective June 1, 2012), pp. 83, 127, at <https://www.sba.gov/sites/default/files/SOP%2050%2010%205%28E%29%20%285-16-2012%29%20clean.pdf>.

¹⁵⁷ SBA, Office of Congressional and Legislative Affairs, correspondence with the author, February 21, 2014.

¹⁵⁸ SBA, "Announcement of SBA Export Express – a New Pilot Loan Guaranty Program for Exporters," 65 *Federal Register* 60491, October 11, 2000; and SBA, "Export Express Pilot Program," 70 *Federal Register* 56962-56963, September 29, 2005.

legislation, subject to reauthorization, in 2010 (P.L. 111-240, the Small Business Jobs Act of 2010).

The Export Express program is designed to increase the availability of credit to current and prospective small business exporters that have been in business, though not necessarily in exporting, for at least 12 full months, particularly those small businesses needing revolving lines of credit.¹⁵⁹ Export Express loans may not be used to finance overseas operations, except for the marketing and/or distribution of products/services exported from the United States.¹⁶⁰

The program is generally subject to the same loan processing, making, closing, servicing, and liquidation requirements as well as the same maturity terms, interest rates, and applicable fees as the SBA Express program. Two key differences between the two programs is that the Export Express program's maximum loan amount is up to \$500,000, and its guaranty rate is 90% for loans of \$350,000 or less, and 75% for loans exceeding \$350,000.

There were 80 lenders with approved SBA Export Express loan guaranties in FY2014. These lenders are located in 31 states, Guam, and Puerto Rico.¹⁶¹ In FY2014, 58 lenders made 124 Export Express loans to 108 small businesses.¹⁶²

Community Advantage 7(a) Loan Initiatives

The SBA's Community Advantage 7(a) loan initiative became operational on February 15, 2011.¹⁶³ It is designed to increase lending to underserved low- and moderate-income communities. The Community Advantage initiative offers a streamlined application process for loans of up to \$250,000. It, along with the now discontinued Small Loan Advantage program,¹⁶⁴ replaced the Community Express Pilot Program, which was also designed to increase lending to

¹⁵⁹ The 12-month in business requirement can be waived if "the applicant's key personnel have clearly demonstrated export expertise and substantial previous successful business experience, and the lender processes the Export Express loan using conventional commercial loan underwriting procedures and does not rely solely on credit scoring or credit matrices to approve the loan." See SBA, "SOP 50 10 5(H): Lender and Development Company Loan Programs," (effective May 1, 2015), p. 108, at https://www.sba.gov/sites/default/files/sops/SOP_50_10_5_H_FINAL_FINAL_CLEAN_5-1-15.pdf.

¹⁶⁰ *Ibid.*, pp. 108, 122.

¹⁶¹ SBA, "Export Express Program Lenders," at <https://www.sba.gov/content/lenders-participating-sba%27s-export-express-program-0>.

¹⁶² SBA, *Fiscal Year 2016 Congressional Budget Justification and FY 2014 Annual Performance Report*, p. 72.

¹⁶³ SBA, "Small Loan Advantage," at <https://www.sba.gov/offices/headquarters/oca/resources/14835>; and SBA, "SBA Announces New Initiatives Aimed at Increasing Lending in Underserved Communities," December 15, 2010, at <https://www.sba.gov/content/sba-announces-new-initiatives-aimed-increasing-lending-underserved-communities>.

¹⁶⁴ The SBA's Small Loan Advantage (SLA) program also became operational on February 15, 2011. It provided a streamlined application process for 7(a) loans of up to \$350,000 (initially \$250,000) if the loan received an acceptable credit score from the SBA prior to the loan being submitted for processing. The program provided the same loan guaranty rate as that of the 7(a) program on loan amounts up to \$350,000 (85% for loans up to \$150,000 and 75% for those greater than \$150,000) and loan proceeds could be used for the same purposes as those of the 7(a) program. The borrower's interest rate was negotiable with the lender, subject to the same maximum rate limitations as those of the 7(a) program. Initially, the SLA program was restricted to PLP lenders. The program was expanded to all SBA lenders on June 1, 2012. The SBA adopted the SLA application process as the model for processing all non-export 7(a) loans of \$350,000 or less, effective January 1, 2014.

underserved communities. It was created by the SBA in May 1999 and ended on April 30, 2011.¹⁶⁵

The Community Advantage pilot initiative 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 loans.”¹⁶⁶ These mission-focused financial institutions include “Community Development Financial Institutions, SBA’s Certified Development Companies and SBA’s nonprofit microlending intermediaries.”¹⁶⁷ 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.”¹⁶⁸

As of February 10, 2015, there were 90 approved Community Advantage lenders, and 57 of them had issued at least one Community Advantage loan. As of February 10, 2015, these 57 active lenders had approved 1,124 Community Advantage loans amounting to \$147.9 million.¹⁶⁹

The initiative was originally announced as a three-year pilot program (through March 15, 2014) and was subsequently extended through March 15, 2017.¹⁷⁰ It provides the same loan guaranty as that of 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 those of the 7(a) program: expansion, renovation, new construction, purchase of land or buildings, purchase of equipment, fixtures, and lease-hold improvements, working capital, refinance debt for compelling reasons, seasonal line of credit, and inventory. The loan terms and guaranty fees are also the same as those of the 7(a) program.¹⁷¹ The loan’s maximum interest rate is prime, plus 6%.¹⁷² 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 days to 10 days.¹⁷³

¹⁶⁵ 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 SBA, “Community Express Pilot Program,” *75 Federal Register* 80562, December 22, 2010.

¹⁶⁶ SBA, “Advantage Loan Initiatives,” at <http://www.sba.gov/advantage>.

¹⁶⁷ Ibid.

¹⁶⁸ Ibid.

¹⁶⁹ SBA, Office of Congressional and Legislative Affairs, correspondence with the author, February 10, 2015. Of the \$147.9 million in approved Community Advantage loans, \$106.795 million had been disbursed as of February 10, 2015.

¹⁷⁰ SBA, “Community Advantage Pilot Program,” *77 Federal Register* 67433, November 9, 2012.

¹⁷¹ SBA, “Advantage Loan Initiatives,” at <https://www.sba.gov/advantage>.

¹⁷² SBA, “Community Advantage Participant Guide,” p. 18, at https://www.sba.gov/sites/default/files/files/Community%20Advantage%20Participant%20Guide%203_0%20%28Final%20Version%2011-13-2012%29.pdf; and SBA, “Community Advantage Pilot Program,” *77 Federal Register* 6619, February 8, 2012.

¹⁷³ SBA, “Community Advantage,” at <https://www.sba.gov/offices/headquarters/oca/resources/14836>.

The SBA has indicated that the Community Advantage initiative’s goal is to “leverage the experience these institutions already have in lending to minority, women-owned and start-up companies in economically challenged markets, along with their management and technical assistance expertise, to help make their borrowers successful.”¹⁷⁴

Author Contact Information

Robert Jay Dilger
Senior Specialist in American National Government
rdilger@crs.loc.gov, 7-3110

¹⁷⁴ SBA, “SBA Announces New Initiatives Aimed at Increasing Lending in Underserved Communities,” December 15, 2010, at <https://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 <https://www.sba.gov/content/community-advantage-approved-lenders>.