



Small Business Provisions in the American Recovery and Reinvestment Act of 2009

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Summary

The American Recovery and Reinvestment Act of 2009 (ARRA, P.L. 111-5), which was signed into law on February 17, 2009, makes supplemental appropriations for many federal programs in an effort to mitigate the effects of the economic recession that began in December 2007. This report provides an overview of key provisions related to the Small Business Administration (SBA). The new law

- Provides an additional \$630 million for loans and loan guarantees divided into two categories: \$375 million is set aside for reimbursements, loan subsidies and loan modifications related to certain loans, and \$255 million for loan guarantees of \$35,000 or less in a new small business stabilization program (BSP);
- Provides \$24 million for microloan technical assistance, and \$20 million to improve lender oversight;
- Provides an additional \$6 million for direct loans;
- Provides an additional \$15 million for the SBA's surety bond program and increases the size of the maximum bond;
- Eliminates (or reduces as much as possible) fees in the SBA's main business loan programs and for lender oversight;
- Allows the SBA to guarantee certain loans that, in part, refinance existing business loans;
- Authorizes the SBA to guarantee pools of first lien CDC/504 loans sold to third party investors; and
- Makes changes to encourage SBA-licensed Small Business Investment Companies (SBICs) to invest more venture capital in small businesses.

Most of the new programs will sunset February 17, 2011, two years after enactment.

This report will be updated as warranted.

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Small Business Provisions in American Recovery and Reinvestment Act of 2009

The American Recovery and Reinvestment Act of 2009 (ARRA) provides additional appropriations for the Small Business Administration (SBA) and makes changes to small business programs with the goal of making the SBA's programs more effective in the current recession. The act

- Provides an additional \$630 million for loans and loan guarantees divided into two categories: \$375 million is set aside for reimbursements, loan subsidies and loan modifications related to certain loans, and \$255 million for loans of \$35,000 or less in a new small business stabilization program (BSP);
- Provides an additional \$69 million for salaries and expenses, including \$24 million for microloan technical assistance, and \$20 million to improve lender oversight;
- Provides an additional \$6 million for direct loans;
- Provides an additional \$15 million for the SBA's surety bond program and increases the size of the maximum bond;
- Eliminates (or reduces as much as possible) fees in the 7(a) and 504 business loan programs and for lender oversight;
- Allows the SBA to guarantee certain loans that, in part, refinance existing business loans;
- Authorizes the SBA to guarantee pools of first lien CDC/504 loans sold to third party investors;
- Increases the funds ("leverage") available to SBA-licensed Small Business Investment Companies (SBICs);
- Requires SBICs to invest at least 50% of their venture capital in low-income areas as defined by the New Market Venture Capital program; and
- Requires SBICs to make 25% of their investments in "smaller" companies.¹

SBA Loan Programs—Additional Funding, Increased Loan Guarantees, and Fees

ARRA provides \$630 million to the SBA to guarantee private sector loans to small businesses: \$6 million for direct loans, and increased SBA guarantees on certain types of loans. The \$630 million is for two purposes: \$375 million is for reimbursements, loan subsidies and loan

¹ "Smaller enterprise" is defined in 15 U.S.C. 662(12) as having a net financial worth of not more than \$6 million and an average net income for the past two years of not more than \$2 million. For additional information on SBA programs, see CRS Report RL33243, *Small Business Administration: A Primer on Programs*, by N. Eric Weiss.

modifications related to SBA 7(a) loans; and \$255 million is for a new small business stabilization program.² For comparative purposes, in FY2008, the SBA had \$786 million in non-disaster loan new budget authority, so ARRA nearly doubles the amount of funding for FY2009.

ARRA authorizes the SBA to increase the percentage of a loan that it guarantees from 75%-80% to 90% in its two major business loan programs (the 7(a) working capital loans and Section 504/Certified Development Company fixed capital loans). The maximum amount guaranteed to a borrower is unchanged.

The 7(a) program guarantees loans made by private sector lenders to small businesses.³ The maximum 7(a) loan guarantee percentage is increased to 90%, the maximum dollar guarantee remains unchanged at \$1.5 million, which reduces the maximum loan under the program to less than \$1.7 million.⁴ Currently, the maximum loan amount is \$2 million. Some SBA loan guarantee programs do not guarantee the maximum percentage allowed by law.

The SBA Certified Development Company/504 program guarantees loans in financing packages made to small businesses for real estate, machinery, or equipment through a combination of Certified Development Companies (CDCs) and private lenders.⁵ A CDC is a nonprofit corporation established with the objective of contributing to community economic development, and the SBA reports that there are 270 CDCs throughout the country.

A typical CDC/504 SBA loan package includes a first lien from a private lender for up to 50% of the cost of the loan, and 40% obtained through a second lien from a CDC. SBA guarantees the CDC's loan. The small business is required to provide at least 10% in equity for the project. The maximum loan guarantee under 504 loans is \$1.5 million, depending on job creation criteria or community economic development, or up to \$4.0 million if it meets other criteria. Section 504 loans cannot be used for working capital or inventory.

Fees in the 7(a) and CDC/504 loan guarantee programs are to be eliminated or reduced as much as possible through September 30, 2010.

The impact of the reduced fees will be to make SBA guarantees more attractive to small businesses seeking loans, but current economic conditions may offset this increase. Reducing the cost of borrowing will increase the demand for SBA-guaranteed loans compared to what demand would have been otherwise. Nevertheless, the recession is likely to reduce small businesses' demand for loans because spending on expansion or modernization is inherently cyclical.⁶

² The SBA guarantees certain loans made to American small businesses by commercial lenders. It is named after Section 7(a) of the Small Business Act of 1953 (P.L. 85-536) as amended.

³ The SBA is not presently using its authority to make 7(a) loans directly to small businesses.

⁴ The \$1.5 million guarantee limit is at 15 U.S.C. 636(a)(3)(B).

⁵ The CDC/504 loan program is named after Section 504 of the Small Business Investment Act of 1958 (P.L. 85-669), as amended, which authorized the program.

⁶ For more information, see CRS Report RL34400, *Economic Factors Affecting Small Business Lending and Loan Guarantees*, by N. Eric Weiss.

Increasing the SBA's guarantee will increase commercial lenders' willingness to provide loans, all else equal, as it tends to reduce lenders' risks, but there is also evidence that lenders are becoming more cautious and are tightening lending standards.⁷

Systemically Important Secondary Market Broker-Dealers

ARRA directs the SBA to work with the Federal Reserve and Treasury to determine how to designate Systemically Important Secondary Market (SISM) Broker-Dealers that will be eligible to receive below market interest rate loans to purchase SBA-guaranteed loans made by others.⁸ The SBA is to create a new office for SISM broker-dealers, appoint a Director, and hire staff.

A secondary market for SBA loans already exists, and by some media estimates, there are as many as 10 major broker-dealers.⁹ Broker-dealers that are not systemically important could be at a competitive disadvantage to those that can get below-market rate loans from the federal government. The new SBA lending facility for SISM broker-dealers has several features. First, loans must be used solely to finance the government-guaranteed portion of SBA loans. Second, loans must be fully collateralized by the SBA-guaranteed portion of the original loans. Third, there is no limit to the frequency or number of times a SISM broker-dealer can obtain a loan. Fourth, there is no limit on the size of a loan, all of which is left to the discretion of the SBA Administrator's office. Fifth, the interest on these loans cannot exceed the Federal Funds target rate plus 25 basis points (0.25%). On December 16, 2008, the Federal Reserve set a target federal funds rate of 0 to 25 basis points (0% to 0.25%), which would have set an interest ceiling of 25 to 50 basis points (0.25% to 0.50%) compared to the Treasury's cost of borrowing, which as of February 13, 2009, ranged from 0.23% for one-month to 0.97% for two-year bonds.¹⁰ Treasury will lose money if it lends funds for less than its cost of borrowing money.

The intent of this portion of the act is to enhance the existing secondary market for SBA loans. The Federal Reserve has developed the Term Asset-Backed Securities Loan Facility (TALF), which supports the issuance of asset-backed-securities collateralized, in part, by SBA guaranteed loans.¹¹ These two programs are to weigh the benefits of providing liquidity to the secondary market for SBA loans against the risks that collateralized debt carries and higher default rates due to an economic downturn. The act does not include specific underwriting standards for SISM

⁷ U.S. Federal Reserve, Board of Governors, "The January 2008 Senior Loan Officer Opinion Survey on Bank Lending Practices," press release, February 4, 2008, <http://www.federalreserve.gov/boarddocs/SnLoanSurvey/200801/default.htm>.

⁸ The SBA secondary market refers to the market for the purchase and sale of loans made or guaranteed by the SBA. SBA broker-dealers are companies that buy and sell the government guaranteed portion of loans, or pools of loans, originated, underwritten, and closed under the Small Business Act. Systemically important refers to major securitizers of SBA loans in the secondary market.

⁹ Emily Flitter, "Bill May Produce New Role for the Fed: Gauging Systemic Risk," *American Banker*, February 3, 2009, p. 5.

¹⁰ U.S. Department of Treasury, *Daily Treasury Yield Curve Rates*. Available at <http://www.ustreas.gov/offices/domestic-finance/debt-management/interest-rate/yield.shtml>.

¹¹ U.S. Federal Reserve, Board of Governors, "Federal Reserve Releases Additional Terms and Conditions of the Term Asset-Backed Securities Loan Facility (TALF)," press release, February 6, 2009, <http://www.federalreserve.gov/newsevents/press/monetary/monetary20081125a1.pdf>.

broker-dealer loans, although it specifies that only the government guaranteed portion of loans in a SISM broker-dealer's inventory can be used as collateral for such new guarantees.

The SISM broker-dealer loan authority will expire February 17, 2011, two years after enactment.

CDC/504 Secondary Market Guarantee Authority

ARRA authorizes the SBA to create an SBA Secondary Market Guarantee Authority to guarantee the loan portion CDC/504 loan pools that are sold to third-party investors.

As a condition to obtain this guarantee, a CDC/504 lender must retain at least 5% of the financing pool and must cover any losses from monthly cash flows. The SBA can charge a maximum monthly fee of 50 basis points (one-half of one percent) on the outstanding balance. On an annual basis, the 50 basis points are equivalent to 6% of the average balance. SBA is limited to guaranteeing up to \$3 billion of pools under this authority.

This authority expires February 17, 2011, two years after enactment.

Refinancing Business Loans

ARRA allows the SBA to refinance existing loans as part of a new CDC/504 loan if the refinancing is less than half of the loan and meets other conditions. Prior law prohibited the use of CDC/504 loans to refinance an existing debt.

The job creation goal for the CDC/504 loan program is reduced from one job for each \$50,000 borrowed to one job for each \$65,000 borrowed. The new goal requires more than 15 jobs to be created for a \$1 million loan. Prior to ARRA, 20 new jobs were required.

The refinancing program and reduced job creation goal are permanent.

Increasing Small Business Investment

ARRA increases the maximum amount of outstanding leverage made available to small business investment companies (SBICs). This act allows an SBIC to leverage up to the lesser of 300% of its private capital or \$150 million. Presently the private capital level ranges from \$15 to \$75 million.¹² The maximum amount of outstanding leverage for two companies licensed jointly is \$225 million.

This provision is permanent.

¹² 15 U.S.C. 683(b)(2).

Business Stabilization Program

ARRA creates a new Business Stabilization Program to guarantee loans of \$35,000 or less to allow small businesses to make up to six months of payments on existing loans. The new loans are to be paid off over five years or less starting one year after the loan is made. The new loans carry no interest, have no fees, and may accept a secondary lien as collateral.

The authority to guarantee new BSP loans terminates September 30, 2010.

GAO Report

Section 507 of ARRA requires the Government Accountability Office (GAO) to report to Congress, within 60 days of enactment of the act, on the actions of the SBA Administrator to implement ARRA. The GAO report is required to include an assessment of the SBA secondary market.

Summary of Programs

Table 1 provides a summary of SBA programs that will receive supplemental funding under ARRA. In addition to \$630 million for loan guarantees and loan subsidies, ARRA provides \$69 million in salaries and expenses, \$10 million for the Office of Inspector General, \$15 million for the Surety Bond Guarantee Revolving Fund, and \$6 million in direct loans.

Table 1. ARRA funding for SBA Programs

amounts in millions of dollars

Program	Level of Funding Under ARRA
Salaries and Expenses	\$69
<i>Marketing, management, and technical assistance for microloans</i>	\$24
<i>Information technology systems</i>	\$20
Office of Inspector General	\$10
Surety Bond Guarantees Revolving Fund	\$15
Direct Loans	\$6
Loan Guarantees	\$630
<i>Reimbursements, loan subsidies and loan modifications for SBA 7(a) loans</i>	\$375
<i>Loan subsidies and loan modifications for loans to small business concerns</i>	\$255

Source: American Recovery and Reinvestment Act of 2009, P.L. 111-5.

Notes: Programs in italics represent sub-components.

Legislative History

Representative David R. Obey introduced H.R. 1, the American Recovery and Reinvestment Act of 2009, in the 111th Congress on January 26, 2009. On January 28, 2009, the House approved the proposed legislation by a vote of 244-188. On February 10, 2008, the Senate passed an amended version of the bill by a vote of 61-37. A conference report (H.Rept. 111-16) was filed on February 12, 2009. On February 12, 2009, the House agreed to the conference report by a vote of 246-183, and on the same date the Senate agreed by a vote of 60-38. The President signed the bill into law on February 17, 2009.

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