

September 8, 2023

The Honorable Roger Williams
Chairman
Committee on Small Business
United States House of Representatives
Washington, D.C. 20515

The Honorable Nydia Velázquez
Ranking Member
Committee on Small Business
United States House of Representatives
Washington, D.C. 20515

Dear Chairman Williams and Ranking Member Velázquez:

As the leading organizations representing virtually all the thousands of lenders participating in the U.S. Small Business Administration (SBA) 7(a) loan program, we write to strongly encourage you to work toward a bipartisan solution in response to issues arising from recent policy changes made to the 7(a) program by SBA, and to identify the lending industry's priorities and concerns as you consider the best path forward. This is especially timely ahead of the scheduled September 14 markup in the House Committee on Small Business slated to consider such legislation.

We support the mission of the 7(a) program to encourage lenders to provide loans to underserved small businesses. However, we remain concerned that SBA's decision to lift the moratorium on the number of non-Federally regulated lenders in the 7(a) program while simultaneously loosening underwriting standards may negatively impact the performance of 7(a) loans, threaten the integrity of the program, and lead to increased borrower and lender fees.¹

As an industry, we have well documented these concerns and urged Congress to take swift action to prevent serious risk to the program and to small business borrowers across the country. Our organizations have called for legislative action, dating back to a joint letter sent to both the Senate and House Small Business Committees on December 1, 2022, shortly after the sweeping rule changes were first proposed. We appreciate that the Senate Committee on Small Business & Entrepreneurship recently passed out of markup the *Community Advantage Loan Program Act of 2023*, which is a good first step toward crafting a legislative solution.

Collectively, we wanted to identify those policy issues which we believe should be part of any bipartisan solution moving forward. Therefore, we respectfully request that you consider legislation that would:

- Ensure common-sense parity between the 7(a) loan program and the 504 loan program to better serve borrowers and preserve programmatic integrity for all SBA lending programs, including requiring all SBA lending to follow prudent lending and strong underwriting criteria, as well as policies that would maintain that SBA loans are for small businesses, rather than large corporations or investment companies;
- Reinstate the long-established, prudent underwriting criteria for SBA lending and limit the use of credit scoring only to underwrite smaller loans to ensure appropriate underwriting and mitigate risk in the billions of dollars in outstanding loans on the Federal government's balance sheet;

¹ See SBA's recent issuance of Final Rules on *Affiliation and Lending Criteria for the SBA Business Loan Programs* [88 FR 21074] and *Small Business Lending Company (SBLC) Moratorium Rescission and Removal of Requirement for a Loan Authorization* [88 FR 21890], as well as two revised and one newly created Standard Operating Procedures manuals (SOPs) and other program guidance.

- Require SBA to consider a larger corporation's control over a small business to prevent SBA loans benefitting large businesses indirectly;
- Protect the statutory authority already given to lenders under their Preferred Lenders Program (PLP) designation to approve loans with "complete authority to make and close loans with a guarantee from the Administration without obtaining the prior specific approval of the Administration"² by providing extra instruction to SBA that PLP lenders should never be required to submit loans for SBA's eligibility approval;
- Cap the number of Small Business Lending Companies (SBLCs) to prohibit SBA from expanding the number of non-Federally regulated lenders for which it serves as primary regulator to an unlimited number in the future;
- Reinstitute the guardrail around SBLCs which was removed by SBA that limited SBLC lending to 7(a) loans only, a vital protection to ensure SBA can realistically serve as a primary regulator without having to also regulate for an unlimited number and type of other lines of business conducted by a SBLC;
- Clarify that SBA cannot create new types of SBLCs to use as a loophole for Congress authorizing new programs with new policy purposes, including Community Advantage SBLCs;
- Require SBA to create a regulatory framework in the Office of Credit Risk Management (OCRM) that addresses enterprise risk in a structure similar to the Federal regulators to work toward greater parity between those lenders for which SBA serves as the primary regulator and federally-regulated lenders, especially from a regulatory, risk management, and prudent lending perspective;
- Provide additional guardrails and authority for the Office of Credit Risk Management (OCRM) to enhance oversight of non-Federally regulated 7(a) lenders for which SBA serves as the primary regulator;
- Ensure all SBLCs are evaluated on the same terms to avoid any future potential for politicization of selecting SBLC licenses;
- Ensure OCRM has appropriate resources to manage oversight responsibilities given a stagnant set-aside from SBA's Salaries and Expenses line item since FY2014, as well as accounts and IG reviews indicating a resource-depleted office;
- Require that strong credit elsewhere tests are maintained to assure that SBA continues its role as a gap lender and that its loan programs do not compete with conventional small business lending;
- Reinstate the recently removed and well-established SBA's Franchise Directory in order to aid lenders in making loans to franchisees;
- Reinstate the requirement for a Loan Authorization or similar document to give lenders and borrowers the necessary documentation on the terms and conditions governing each individual SBA loan;
- Remove the new Administrator discretion to overturn decisions previously reserved for career staff so as to avoid the potential for politicization of loan denials and denials of servicing actions;
- Provide permanency to the Community Advantage program, which has operated as a pilot program since 2011 aimed at focusing on underserved borrowers;
- Ensure risk mitigation guardrails around the Community Advantage program, including maintaining its public policy mission of providing small loans;
- Prohibit SBA from permitting the sale of the entire unguaranteed portion of any loan sold on the secondary market to ensure appropriate behavior;
- Prohibit direct lending using the 7(a) program authority in the future which would deplete 7(a) authorization, drive up program costs, and disincentivize private-sector partnerships;

² *Small Business Act* [PL 85-536], as amended through P.L. 117-328, Enacted December 29, 2022.

- Reverse a newly SBA-created technology services fee on borrowers that has no upward limit and no requirement to be disclosed to borrowers, a sweeping departure from the typically transparent and reasonable fees in the SBA lending industry; and
- Create guardrails around the now loosened restrictions on same institution debt refinancing in order to maintain programmatic integrity while still maintaining reasonable lender flexibility around an interim advance transaction.

We would note that several issues outlined above are in response to policy concerns presented by the slow drip of additional guidance SBA has been providing through SOPs and other policy guidance released in the wake of the issuance of the final rules. It is important to caution that in order to fully address the concerns presented by the SBA's rulemaking, there must be careful consideration of these SOPs.

Traditionally, SOPs are not intended to promulgate substantive policy changes. Rather, they should simply provide the day-to-day, technical guidance implementing issued regulations. However, the three new SOPs introduced in the wake of the recent rulemaking introduce substantial additional policy changes which were *never* proposed or discussed during the recent rule-change process. These changes pose *further* increased risk to the program on top of the risk already posed by the regulatory changes. We are not advocating for overly prescriptive legislation on technical guidance that is best reserved for SOPs. However, some of these substantive policy shifts found only in the SOPs should be part of the legislative conversation simply because, unfortunately, they are *not* technical in nature.

To give you a sense of the sheer scope of the very recent SBA changes, here is the laundry list of final changes released by the agency for the first time over the course of roughly one month:

Final Rules and Federal Register Notification

- *Final Rule on Affiliation and Lending Criteria for the SBA Business Loan Programs [88 FR 21074, effective 5/11/2023]*
- *Final Rule on Small Business Lending Company (SBLC) Moratorium Rescission and Removal of Requirement for a Loan Authorization [88 FR 21890, effective 5/12/2023]*
- *Notification on Small Business Lending Company Application Process [88 FR 32623, effective 5/22/2023]*

Notices

- *Implementation of Final Rule on Affiliation and making other program changes [5000-846607, dated 5/9/2023, reg effective 5/11/2023]*
- *Removal of Loan Authorization [5000-846991, dated 5/9/2023, reg effective 5/12/2023]*
- *Revision to notice regarding removal of Loan Authorization [5000-847482, dated 5/26/2023]*
- *Issuance of SOP 50 10 7 [5000-847027, dated 5/10/2023, SOP effective 8/1/2023]*
- *Issuance of SOP 50 57 3 [5000-846632, dated 5/31/2023, SOP effective 8/1/2023] [actual SOP made available 6/14/2023]*
- *Conversion of CA lenders to CA SBLCs [5000-846918, dated 5/1/2023, reg effective 5/12/2023]*

SOPs

- *SOP 50 10 7, Lender and Development Company Loan Programs, issued 5/11/2023, effective 8/1/2023*
- *NEW SOP 50 56 1, Lender Participation Requirements, posted on SBA website 6/14/2023, effective 8/1/2023 (released without an accompanying notice)*
- *SOP 50 57 3, 7(a) Loan Servicing and Liquidation, posted on SBA website 6/14/2023, effective 8/1/2023*

While we understand and fully support SBA's stated goals of aiding underserved borrowers, we remain concerned that SBA's changes do not meet those goals and may, in fact, create the potential for serious risk to SBA loan program integrity and to borrowers. The recent rule and SOP changes erode the reliance upon decades-long prudent SBA lending standards, which have ensured acceptable loss rates and have kept program costs down for the very borrowers we all aim to aid while avoiding the need for a taxpayer subsidy. In addition, by allowing a potentially unlimited number of non-Federally regulated lenders to enter the 7(a) loan program while telling these same lenders to "do what you do" for similar conventional loans, the new underwriting guidance from SBA to the lending community, creates an uneven playing field among regulated and non-Federally regulated lenders. And while SBA stipulates that it will serve as primary regulator for this non-Federally regulated lender expansion, the available evidence points to the opposite in terms of SBA's capacity to be a prudential regulator, since the agency lacks both resources and a regulatory framework to oversee lending entities at a holistic, institutional-risk level. And the most devastating borrower impact of these changes? Removing prudent lending guardrails opens the door to the potential for small business borrowers to receive loans they cannot repay—a crippling consequence for these borrowers.

We are greatly encouraged that it appears both the lending industry and Congress are united in pushing back on these sweeping changes. Collectively, we urge the Committee to craft a comprehensive legislative solution that can serve as a bicameral path forward, using many of the underlying provisions in the Senate Committee's bill on these issues while building upon and improving some of those provisions.

Our trade associations look forward to continuing to work with Congress through the legislative process. We will continue to give voice to the lending industry's concerns regarding how best to maintain 7(a) loan program integrity. Supporting small businesses, especially those businesses that rely upon SBA-guaranteed financing, is of utmost importance to our national economy and our organizations stand ready to assist in ensuring that access to capital is protected. Thank you for your consideration of the priorities and concerns which we have laid out as you move forward in the legislative process.

Sincerely,

Consumer Bankers Association (CBA)

Credit Union National Association (CUNA)

Independent Community Bankers of America (ICBA)

National Association of Federally-Insured Credit Unions (NAFCU)

National Association of Government Guaranteed Lenders (NAGGL)

Cc: The Honorable Ben Cardin
The Honorable Joni Ernst