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106TH CONGRESS, 1st Session | HOUSE OF REPRESENTATIVES | REPORT 106–12

TECHNICAL CORRECTIONS TO MICROLOAN PROGRAM

FEBRUARY 8, 1999.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. TALENT, from the Committee on Small Business, submitted the following

REPORT

[To accompany H.R. 440]

[Including cost estimate of the Congressional Budget Office]

The Committee on Small Business, to whom was referred the bill (H.R. 440) to make technical corrections to the Microloan Program, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

PURPOSE

The purpose of H.R. 440 is to make certain technical corrections to the microloan program at the Small Business Administration and to improve the loan loss reserve requirement established for intermediaries operating under that program.

The microloan program was established as a pilot program in 1991 and was made permanent in 1997. The microloan program provides small loans, under $25,000, to the nation's smallest entrepreneurs. These loans are made through intermediaries, SBA certified and approved non-profit lending and business development organizations. These intermediaries borrow funds from the SBA and, in turn, lend those funds to small businesses. In order to protect taxpayer assets the intermediaries are required to maintain a loss reserve based on the amount of microloans they have outstanding.

NEED FOR LEGISLATION

The microloan program was made permanent on December 2, 1997 as a provision of P.L. 105–135, the Small Business Reauthorization Act of 1997. At that time, changes were also implemented to modify the loan loss reserve for microloan intermediaries. The

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loan loss reserve language in P.L. 105–135 specified that microloan borrowers were required to maintain a loss reserve of 15 percent of their outstanding microloans for the first five years of their participation in the program. After that, intermediaries were to be required to maintain a loss reserve equal to 10 percent of their outstanding loans or twice their loss rate, whichever was greater.

Unfortunately, this provision was interpreted by the SBA to mean an amount equal to twice an intermediary's aggregate losses. For example: If an intermediary had average annual losses of five percent over five years the SBA would not impose a loss reserve of ten percent (twice the annual rate) as intended by the Congress. They would instead impose a loss reserve of fifty percent (twice the aggregate annual losses over five years).

This interpretation created an immense burden on microloan intermediaries. As a result, at the end of the 105th Congress, the Senate Committee on Small Business added language similar to H.R. 440 to H.R. 3412 to remedy the situation. Unfortunately, this language, as part of the larger bill, failed to pass the Congress before adjournment.

Shortly thereafter, the Chairmen of the House and Senate Committees on Small Business, Representative James M. Talent and Senator Christopher Bond, and their colleagues, Representative Nydia Velazquez and Senator John Kerry, the Ranking Democratic members of the Committees, wrote to SBA Administrator Aida Alvarez requesting her forbearance in applying the loan loss regulations. (A copy of that letter is attached as an Appendix.)

H.R. 440 will correct this interpretation and clearly establish that the loan loss reserve will be fifteen percent for the first five years for all intermediaries, and that intermediaries may apply for a reduction of the reserve to reflect their actual annual average loss rate, but no less than ten percent.

The loan loss reserve reduction is to be based on the actual annual average loss rate over a five year period. The Committee expects that intermediaries will request such reviews no more than annually, and that such reviews will not affect the SBA's ability to conduct further reviews for oversight and management purposes.

H.R. 440 also replaces the cap on the amount of microloan funds that can be made available to intermediaries in any one State. This cap was originally imposed to ensure that microloan funds would not be used disproportionately in those States with more aggressive microloan programs. As the program has matured, however, this restriction has become unnecessary. The Committee now finds that it would be more useful to establish a limited guarantee of the availability of funds for all States. The availability of these funds is subject to their availability through appropriations, and the approval of the SBA of the request for funding. In addition, the Committee expects any reserve established by the SBA to be held for no more than the first half of the fiscal year.

COMMITTEE ACTION

During the 105th Congress the Committee on Small Business passed H.R. 3412, a bill to make technical corrections to the Small Business Investment Company Program. This bill passed the House of Representatives on March 24, 1998. When it passed the

Senate, on September 30, 1998, it included language substantially similar to H.R. 440. Unfortunately, H.R. 3412 was not taken up again by the House during the 105th Congress due to time constraints.

H.R. 440 was introduced on February 2, 1999. On February 3, 1999, the Committee on Small Business met for purpose of marking up and reporting H.R. 439 and H.R. 440. H.R. 440 was introduced, considered as read, and opened for amendment. No amendments were offered. Chairman Talent then moved to pass H.R. 440 and report it to the House. At 2:50 p.m., by a unanimous voice vote, a quorum being present, the Committee passed the bill, H.R. 440, and ordered it reported.

SECTION-BY-SECTION ANALYSIS

SECTION 1. SHORT TITLE

This act may be cited as the "Microloan Program Technical Corrections Act of 1999".

SECTION 2. TECHNICAL CORRECTIONS

This section eliminates the language in paragraph 7(m)(7)(B) restricting the amount of loan funds made available to any single state, and replaces it with language requiring SBA to maintain a minimum amount ($800,000) of funding available each year for each State's intermediaries. This amount is subject to available appropriations and the approval of the Small Business Administration. Any funds that are reserved by the SBA for the purposes of this provision may be released at the beginning of the third fiscal quarter.

This section also inserts language requiring SBA to not only select and approve intermediaries but also make sure that some funding is available to them.

SECTION 3. LOAN LOSS RESERVES

This section changes the loan loss reserve required to be established by microloan intermediaries. The loss reserve provides a hedge for the SBA against the failure of an intermediary.

Under the new language all intermediaries will be required to have a 15 percent loss reserve for their first five years. After five years intermediaries may request a review by the SBA. Existing intermediaries may request a review based on the most recent five year period. If an intermediary's five year average annual loss rate is lower than 15 percent then the SBA may reduce the loss reserve requirement for the intermediary, but no lower than 10 percent. The request for a review is to be an annual review. However, this review is not to be interpreted to preclude any reviews initiated by the SBA for the purposes of program oversight.

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, February 4, 1999.

Hon. JAMES M. TALENT,
Chairman, Committee on Small Business,
House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 440, the Microloan Program Technical Corrections Act of 1999.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Mark Hadley.

Sincerely,

(For Dan L. Crippen, Director).

Enclosure.

H.R. 440—Microloan Program Technical Corrections Act of 1999

CBO estimates that enacting this bill would not have a significant effect on the federal budget. Assuming the availability of appropriated funds, we estimate the Small Business Administration (SBA) would spend less than $500,000 to review the requirements for loan loss reserves of microloan intermediaries. Because enactment of this bill would not affect direct spending or receipts, pay-as-you-go procedures would not apply.

Under the microloan program, SBA provides grants, loans, and loan guarantees to nonprofit organizations, which act as intermediaries and use the funds to provide small businesses with technical assistance and loans ranging from $100 to $25,000. The bill would eliminate a provision of current law that limits the amount of loan funds that intermediaries within a single state can receive under the microloan program. H.R. 440 also would clarify the requirements for loan loss reserves of intermediaries. Current law requires intermediaries to maintain loan loss reserves equal to 15 percent of their notes receivable. The bill would permit SBA to reduce the requirements for loan loss reserves for those intermediaries with historical loss rates of less than 15 percent during the previous five years. Finally, H.R. 440 would set the requirement for loan loss reserves to be no less than 10 percent and no more than 15 percent. Changing the requirement for loan loss reserves could affect the subsidy rate for the microloan program, but any such effect would be negligible.

H.R. 440 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act and would not have a significant impact on the budgets of state, local, or tribal governments.

The CBO staff contact is Mark Hadley. This estimate was approved by Robert A. Sunshine, Deputy Assistant Director for Budget Analysis.

COMMITTEE ESTIMATE OF COSTS

Pursuant to the Congressional Budget Act of 1974, the Committee estimates that the amendments to Small Business Act in H.R. 440 will not increase appropriations over the next five fiscal years. Furthermore, pursuant to clause 3(d)(2)(A) of rule XIII of the Rules of the House of Representatives, the Committee estimates that implementation of H.R. 440 will not significantly increase administrative costs. This concurs with the estimate of the Congressional Budget Office.

OVERSIGHT FINDINGS

In accordance with clause 4(c)(2) of rule X of the Rules of the House of Representatives, the Committee states that no oversight findings or recommendations have been made by the Committee on Government Reform with respect to the subject matter contained in H.R. 440.

In accordance with clause 2(b)(1) of rule X of the Rules of the House of Representatives, the oversight findings and recommendations of the Committee on Small Business with respect to the subject matter contained in H.R. 440 are incorporated into the descriptive portions of this report.

STATEMENT OF CONSTITUTIONAL AUTHORITY

Pursuant to clause 3(d)(1) of rule XIII of the Rules of the House of Representatives, the Committee finds the authority for this legislation in Article I, Section 8, Clause 18 of the Constitution of the United States.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

SECTION 7 OF THE SMALL BUSINESS ACT

SEC. 7. (a) * * *

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(m) MICROLOAN PROGRAM.—

(1) * * *

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(3) LOANS TO INTERMEDIARIES.—

(A) * * *

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[(D) LOAN LOSS RESERVE FUND.—The Administration shall, by regulation, require each intermediary to establish a loan loss reserve fund, and to maintain such reserve fund until all obligations owed to the Administration under this subsection are repaid. The Administration shall require the loan loss reserve fund to be maintained—

[(i) during the initial 5 years of the intermediary's participation in the program under this subsection, at a level equal to not more than 15 percent of the outstanding balance of the notes receivable owed to the intermediary; and

[(ii) in each year of participation thereafter, at a level equal to not more than the greater of—

[(I) 2 times an amount reflecting the total losses of the intermediary as a result of participation in the program under this subsection, as determined by the Administrator on a case-by-case basis; or

[(II) 10 percent of the outstanding balance of the notes receivable owed to the intermediary.]

(D)(i) IN GENERAL.—The Administrator shall, by regulation, require each intermediary to establish a loan loss reserve fund, and to maintain such reserve fund until all obligations owed to the Administration under this subsection are repaid.

(ii) LEVEL OF LOAN LOSS RESERVE FUND.—

(I) Subject to subclause (III), the Administration shall require the loan loss reserve fund of an intermediary to be maintained at a level equal to 15 percent of the outstanding balance of the notes receivable owed to the intermediary.

(II) REVIEW OF LOAN LOSS.—After the initial 5 years of each intermediary's participation in the program authorized by this subsection, the Administrator shall, at the request of the intermediary, conduct a review of the annual loss rate of each intermediary. Any intermediary in operation under this subsection prior to October 1, 1994 that requests a reduction in its loan loss reserve shall be reviewed based on the most recent five year period preceding the request.

(III) REDUCTION OF THE LOAN LOSS RESERVE.—Subject to the requirements of this subclause the Administrator may reduce the annual loan loss reserve requirement to reflect the actual average loan loss rate for the intermediary during the preceding five year period, except that in no case shall the loan loss reserve be reduced to less than 10 percent of the outstanding balance of the notes receivable owed to the intermediary.

A reduction may be allowed only if the intermediary demonstrates to the satisfaction of the Administrator that—

(aa) the average annual loss rate for the intermediary during the preceding 5 year period is less than 15 percent; and

(bb) that no other factors exist that may impair the ability of the intermediary to repay all obligations owed to the Administration under this subsection.

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(7) PROGRAM FUNDING FOR MICROLOANS.—

(A) * * *

[(B) STATE LIMITATIONS.—During any fiscal year, a State shall not receive new loan funds from the Administration that exceed 125 percent of the State's pro rata share of the microloan program authorization during such fiscal year, such share to be based on the population of the State, as compared to the total population of the United States. If, however, at the beginning of the fourth quarter of a fiscal year the Administration determines that a portion of appropriated microloan funds are unlikely to be awarded during that year, the Administration may make additional funds available to a State in excess of 125 percent of the pro rata share of that State.]

(B) AVAILABILITY OF FUNDS.—Subject to appropriations, the Administration shall ensure that at least $800,000 of new loan funds are available for each State in any fiscal year. All funds are to be made available subject to approval of the Administration. If, at the beginning of the third quarter of a fiscal year, the Administration determines that the funds necessary to comply with this provision are unlikely to be awarded that year, the Administration may make those funds available to any State or intermediary.

(8) EQUITABLE DISTRIBUTION OF INTERMEDIARIES.—In approving microloan program applicants *and providing funding to intermediaries* under this subsection, the Administration shall select *and provide funding to* such intermediaries as will ensure appropriate availability of loans for small businesses in all industries located throughout each State, particularly those located in urban and in rural areas.

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APPENDIX

CONGRESS OF THE UNITED STATES,
Washington, DC, December 4, 1998.

Re microloan loan loss reserve.

Hon. AIDA ALVAREZ,
Administrator, U.S. Small Business Administration,
Washington, DC.

DEAR ADMINISTRATOR ALVAREZ: Last year the Senate Committee on Small Business held a hearing on SBA's Microloan program, which was in the last year of its pilot status. As a result of that hearing, and the program's success during its pilot stage, the Committee, and eventually the entire Congress, passed legislation to make the program permanent, to increase substantially the authorized funding levels for loans and technical assistance, and to restructure the loan loss reserve requirement. The purpose of restructuring the loan loss reserve requirement was to enable microloan intermediaries with successful loan portfolios and low loss histories to maintain lower loss reserves and have the ability to use that capital for additional microloans or technical assistance.

Unfortunately, the language as passed was not interpreted in a way that would achieve that purpose. As part of the Senate version of H.R. 3412, the Senate passed a clarification of the 1997 loan loss reserve language, which the Administration supported, but there was insufficient time remaining in the session to consider the clarifying changes and act on them. Therefore, we ask that SBA refrain from implementing the restructured reserve requirement until both houses of Congress have an opportunity to consider the issue and act on it. We expect such action to occur early in the next session.

Thank you for your cooperation in this matter.

Sincerely,

CHRISTOPHER S. BOND,
Chairman, Committee on Small Business, U.S. Senate.

JAMES M. TALENT,
Chairman, Committee on Small Business, U.S. House of Representatives.

JOHN F. KERRY,
Ranking Democrat, Committee on Small Business, U.S. Senate.

NYDIA M. VELAZQUEZ,
Ranking Democrat, Committee on Small Business, U.S. House of Representatives.

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