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UNDER THE MICROSCOPE: REVIEWING KEY SBA PROGRAMS WITH ASSOCIATE ADMINISTRATOR FROST

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES
HOUSE OF REPRESENTATIVES

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WEDNESDAY, MAY 15, 2024

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Committee met, pursuant to call, at 10:00 a.m., in Room 2360, Rayburn House Office Building, Hon. Roger Williams [chairman of the Committee] presiding.

Present: Representatives Williams, Stauber, Meuser, Van Duyne, Salazar, Mann, Ellzey, Molinaro, Alford, Crane, Bean, Lalota, Maloy, Malliotakis, Velázquez, Phillips, Landsman, McGarvey, Gluesenkamp Perez, Scholten, Thanedar, Davids, and Pappas.

Chairman WILLIAMS. We will pray first, and then we'll pledge.

Mr. MEUSER. Lord, thanks for this hearing this morning. Thanks that we all get to live and serve in the greatest country in the world. We pray for all the small businesses out there. We pray for all the folks that have ideas to start small businesses. We pray that governments would assist when it is their priority. We also pray for health concerns for everybody in this room, friends and family as well. We love you and are grateful for you. Now we will do the pledge. I pledge allegiance to the flag of the United States of America. And to the republic for which it stands. One nation, under God, indivisible, with liberty and justice for all.

Chairman WILLIAMS. Good morning, everyone, and I now call the committee on Small Business to order. Without objection the Chair is authorized to declare the recess of the committee at any time. I now recognize myself from my opening statement. I want to welcome you all today's hearing, which will focus on the oversight of the SBA's Office of Credit Risk Management. This office oversees the SBA's lending programs, including the Flagship 7a loan program. And in 2023, this program alone lent over $27 billion to main street businesses. In April of last year, the SBA finalized two rules that make drastic changes to the program, which many Members of this committee have expressed concerns over.

The first rule removed the standardized underwriting procedures for 7a loans. The 7a program allows banks to offer loans to businesses that are on the edge of creditworthiness. In order for the banks to extend these loans, the government backs between 75 percent to 85 percent of the dollar amount. Since the taxpayers are on the hook if enough of these loans go bad, it is very important that there are guardrails in place to businesses that get these loans and

have a realistic chance to pay them back. Unfortunately, the SBA removed the underwriting criteria that allowed the program to run smoothly for decades and is now allowing each individual lender to use their own standards. This will make oversight of the lending activities much more challenging for the agency and increased likelihood of loans going bad. The SBA is reporting that they are seeing an increase in small dollar loans, but at the same time, we have seen a sharp increase in early default rates within this program.

The second rule removed the cap that limited the number of lenders that could participate in the government lending program. Only a few years prior, the SBA determined that it simply did not have the capacity to oversee more lenders. And now, even though the Office of Capital Access had been drastically reduced staffing levels, they changed course and decided to take on more responsibility anyway. So, we have already seen the SBA ignore some warning signs coming from the new lenders within the 7a program. And when SBA administrator Guzman testified to this committee last year. She claimed the SBA has a rigorous application process for the SBLC program. However, that claim is contradicted when seeing the SBA awarded license to Funding Circle. A company that had started operating losses had standard operating losses the year prior to applying for this new license and during the company's recent earning calls, the CEO claimed it would be too costly to get the SBA lending program functional. Because of this, the CEO stated that they are looking to sell this U.S. business line. Even though these comments were made during the application process, the SBA decided to ignore them and approve their license anyway.

The final thing I am looking forward to discussing is the SBA's handling of the EIDL loans under $100,000. The agency abruptly decided to stop collecting on these loans back in 2022, only to change course over a year later. Now, while I am pleased that the agency claims they will start collecting on these loans, I still have many questions about the long term servicing cost of this portfolio, the amount of taxpayer dollars that were lost during the year of inaction, and the estimated recoupment amounts from their efforts. We must ensure that the SBA is being a good steward of Americans tax dollars. Now, lastly, I ask unanimous consent, for Representative Malliotakis, from the great state of New York to waive to the committee for the purpose of asking questions and without objection, that is so ordered.

I want to thank you all again for being here with us today, and I am looking forward to today's conversation. And with all that, I yield to our distinguished Ranking Member from New York, Ms. Velázquez.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman. I would like to start off by thanking Associate Administrator Frost for joining us here this morning. Ms. Frost, welcome to the committee. The COVID-19 pandemic opposed a historic threat to our nation's small businesses. The number of active business owners in the U.S. plummeted by 3.3 million, or 22 percent, over a two month period from April—from February to April 2020. The drop in business owners was the largest on record and losses were felt across all industries. Underserved small businesses were especially hard hit.

African American businesses experienced a 41 percent drop, while Latino business owners fell by 32 percent and Asian business owners fell by 26 percent. Throughout the pandemic, the SBA stepped up and offered small businesses across the country a lifeline. The SBA delivered an unprecedented $1.2 trillion in emergency grants and loans over two years. That funding contributed to a historic economic recovery of 21 million lost private sector jobs, plus 4 million more private sector jobs than existed before the pandemic.

Beginning in early 2021, thanks to the leadership of Administrator Guzman, longstanding anti-fraud controls were reinstituted and new safeguards were put in place to reduce the risk for potential fraud. Since then, the SBA has been actively engaged in reducing the risk of fraud throughout the agency by improving its operation and bolstering its risk management systems. Across all four pandemic relief programs, the SBA has screened 49.3 million applications, identified 4 billion in applications, loans, grants and awards that had had indicators of potential fraud, and blocked 2.46 million applications due to likely fraud. That being said, many of the fraudulent activities that occurred in PPP and the other COVID relief programs were conducted through fintech's. According to a study published by the University of Texas, Austin, 9 of the 10 PPP lenders with the highest rate of suspicious loans were fintech companies, and the most active fintech PPP lenders generated over $1 billion in fees from the SBA.

Given the significant level of fraud conducted by fintech lenders in the PPP, there has been strong bipartisan concern over two final rulemakings by the SBA last year, which weakened the underwriting criteria and loosened affiliation standards in the agency's core lending programs. Most importantly, it lifted the decades old moratorium on the number of SBLCs, potentially opening this program up to fintech lenders. There are still outstanding questions as to one SBLC award to Funding Circle, and I look forward to hearing from Ms. Frost regarding this particular license. The SBA's mission is too important to grant loan making authority to a lender that is not fully committed to its programs. The SBA has been critical to the success of millions of small firms through its over 70 years of existence. Much of that is due to the core lending programs and their ability to reach businesses that have traditionally been locked out of the capital market. I hope to hear more about how Congress can strengthen and improve these programs. Mr. Chairman, I yield back.

Chairman WILLIAMS. The lady yields back and I now will introduce our witness. It is my privilege today to introduce Ms. Katie Frost. Ms. Frost is the Associate Administrator of the Office of Capital Access at the Small Business Administration. And at the SBA, Ms. Frost leads the agency's Office of Capital Access, which oversees major programs like the 7a lending program. Prior to the current position at the SBA, Ms. Frost serves as Deputy Associate Administrator of the Office of Capital Access as well as Policy Advisor and Senior Advisor for the Office of the Administrator. Ms. Frost holds a Bachelor of Arts political science degree from UCLA, the Bruins right?

Ms. FROST. Go Bruins.

Chairman WILLIAMS. And a master's in public policy from Harvard's Kennedy School. Ms. Frost, thank you for joining us. And I am looking forward to today's conversation. And before anything else, I would like to remind you that your oral testimony is restricted 5 minutes in length. And if you see the light turned red in front of you, means your 5 minutes have concluded and you should wrap up your testimony. And if you don't, I will remind you with a little tap on the gavel. Okay? I now recognize Ms. Frost for her 5 minute opening remarks.

STATEMENT OF KATHRYN FROST, ASSOCIATE ADMINISTRATOR, OFFICE OF CAPITAL ACCESS, SMALL BUSINESS ADMINISTRATION

Ms. FROST. Good morning, Chairman Williams, Ranking Member Velázquez, and Members of the committee. On behalf of Administrator Guzman and the entire agency, thank you for the opportunity to appear before you today. I serve as the Associate Administrator for the Office of Capital Access, where I am responsible for the agency's business loan programs, including our 7a, 504 and microloan program, the agency's surety bond program, SBA's direct disaster loan program, and several of our pandemic programs, including the Paycheck Protection Program, the COVID EIDL program, and the Restaurant Revitalization Fund.

Collectively, these programs connect creditworthy small businesses to capital so that they can start, grow and expand resilient businesses. There's never been a better time to start a business than under the Biden Harris administration. Since 2021, we have experienced a small business boom in this country, with more than 17 million Americans filing new business applications, and this is being led by women and people of color. This isn't an accident. It is thanks to intentional policy and program implementation, including improvements to SBA's loan program. SBA has increased lending to Latino owned businesses by 80 percent since the start of the Biden Harris administration, and we have more than doubled SBA loans to black owned businesses since 2020. We have also invested in modern technology like MySBA and the unified lending platform, as well as Lender Match to improve the lender experience, the borrower experience and reduce loan processing times. But one of the persistent problems for small businesses has been accessing capital, especially small dollar loans. These loans tend to be less profitable and harder to get on the conventional market, and small SBA loans, those under $500,000, fell by 40 percent during the previous administration. Reversing this decline has been one of administrator Guzman's top priorities, and beginning in '22 into '23, she modernized SBA loan policy with sweeping reforms to strengthen the network of SBA lenders and to make it a little easier to work with the SBA.

In August of last year, those changes went live. To make it easier to work with SBA, we simplified underwriting requirements for loans under $500,000 so that they align with industry norms. We removed unnecessary frictions, including the complex affiliation rule and complex requirements for documenting equity injection. And at the same time, SBA established the most robust front end fraud control system in the history of the program, something

that's been applauded by our inspector general. To strengthen the network of SBA lenders, we created the new community advantage small business lending company, or CASBLC license, bringing 142 mission-based lenders into the program, and that included 30 new lenders last fall. We also added three new SBLC's for the first time in four decades, each of which has a focus on a particular market gap in SBA lending that includes small dollar loans, lending to native owned businesses and entrepreneurs, and lending in persistent poverty counties and rural areas.

We now have nine months of performance data after the implementation of these reforms, and I am pleased to report on behalf of Administrator Guzman that the changes are working. In fiscal year 2024 to date, SBA has approved 22,000 7a loans under $150,000. That puts us on pace to nearly double the number of small loans approved in the final year of the previous administration. Everyone, that is about 1,000 more small businesses getting a small loan every month compared to just a few years ago. 7a loans under $500,000 are similarly up 25 percent, and community advantage lending is up 17 percent compared to this time last year. For this progress, we give credit to our partners in the lending community. They have embraced this opportunity, and they have seized it to put more money in the hands of America's small businesses.

And yet, despite this notable progress, it is still too hard for many Americans to access capital. The Federal Reserve's 2024 report showed that half of employer firms who sought capital did not receive what they needed. So SBA continues our work to help. In April, our nation celebrated second chance month, and SBA expanded access to our capital programs for returning citizens. In May, we expanded the use of the 504 loan program for projects that reduce energy consumption. And in March, we raised the cap on SBA's surety bond program for the first time in 11 years. The president's 2025 budget establishes a path to deliver on the Small Business Act's long standing directive of directly lending to credit worthy small businesses who are unable to secure credit in the private sector. We have extensive experience with direct disaster lending, including successfully lending nearly $3 billion to over 43,000 borrowers last year. I know there are many other issues you would like to discuss, and I look forward to your questions. Thank you.

Chairman WILLIAMS. Thank you. And now we will move to the Member questions under the 5 minute rule. I recognize myself for 5 minutes. In this year's congressional budget justification, I was disappointed to see that plans that the SBA requested to establish a direct lending program. The SBA is supposed to be the lender of last resort and not compete with the private sector. When the Administrator testified on the Hill last month, she made it clear they would take an act of Congress to set up a direct lending program. So, Ms. Frost, do you agree with the administrator that the SBA will not be able to set up a direct lending program without Congress involvement? And will you commit that you will not take any actions to skirt this statutory check on the SBA's ability to set up the program in the future?

Ms. FROST. The Administrator said during her testimony last month that we would begin a direct lending business program if

given the tools to do so. Of course, we have had a longstanding direct disaster loan program for decades, including lending over $3 billion in the direct disaster loan program last year to about 43,000 borrowers.

Chairman WILLIAMS. The SBA offered two different loan options to small businesses during the COVID-19 pandemic, and the Paycheck Protection Program offered forgivable loans for businesses and was administered with the help of private sector lenders. And the COVID EIDL program offered a long term, fixed rate loan that were distributed with the SBA. That was the main difference. Now, both of these programs helped main street businesses stay afloat during the pandemic. But we now need to reflect on both of these programs to figure out what do we do moving forward on them. So the COVID EIDL portfolio is still staying in the government balance sheet, which equates to over $400 billion. And when an independent consulting firm looked into what to do with this portfolio back in 2021, they said the agency should sell all or a portion of the portfolio.

The agency ignored this advice, and since then, the loans have become less collectible and therefore less valuable to the private sector. The SBA has requested hundreds of millions of dollars from Congress each year to continue servicing these loans. So even though we have requested an analysis of the sale of the EIDL portfolio for months, we have repeatedly been stonewalled and told to just look at the PPP data. Well, we know these programs are fundamentally different, and the comparisons don't even make sense. So I am going to ask you once again, has the agency conducted a new analysis of just the EIDL portfolio to determine if it should be sold? And when will the committee be able to see the analysis.

Ms. FROST. So the PPP and the COVID EIDL programs were both first of their kind, brand new programs. And so, of course, the agency has paid special attention to both programs in terms of finding the best way to manage these loans and responsibly move the programs forward. We are finalizing our analysis on a potential COVID EIDL sale, and we will share that with the committee when it is complete.

Chairman WILLIAMS. Now, when the SBA changed the 7a lending rules, Members of this committee repeatedly voice their concerns that changing the underwriting standards would lead to increased default rates. Now, the data is now starting to come in, and it is very troubling. The early default race currently sits at 0.86 percent, which is over two times higher than the rate one year prior, which was 0.39 percent. So this not only increases the risk the taxpayers have to bail out the program, but it is a death blow to the businesses that attempted to take out a loan to grow their businesses before they were ready. So, Ms. Frost, what recourse does the agency have to reverse this trend? And how will you ensure that lenders are using more stringent underwriting standards to prevent these defaults?

Ms. FROST. So, using modern technology, we are able to keep a constant pulse on our loan programs portfolio and how all of those portfolios are performing. I think it is important to note that during the pandemic, with a lot of government money out in our economy, there was a historically low default rate in our pandemic

programs. And what you are referencing right now, sir, is a regression to the mean, a return to normal, a return to what we saw in the pre pandemic baseline of what we kind of expect as a default rate for our loan programs. We're, of course, keeping an eye on this and other critical metrics. And we have strong oversight of all of our lenders, with appropriate enforcement tools and supervision to ensure that the program stays on track.

Chairman WILLIAMS. Okay. All right. I yield back my time. And now, recognize Ms. Velázquez for her questioning.

Ms. VELAZQUEZ. Thank you, Mr. Chairman. Associate Administrator Frost, in response to a September 2023 IG report, the SBA rerun the analysis for referrals to the Treasury Department for loans for $100,000 or less. Can you explain this analysis and why the SBA changed its referral decision?

Ms. FROST. Absolutely. SBA is a data driven organization, and we are going to make decisions based on the best data available at the time. The initial analysis that was conducted on the collectability of these small dollar loans was conducted in early 2022. Actually, before repayment had even started. So it was modeling, right. Based on some projections. As the data came in, we actually updated that analysis three additional times. And the latest analysis in December of last year showed that it was likely going to be cost effective if we took that final collection step of referring to Treasury. And so we began doing so. And as of today, we have referred over 920,000 COVID EIDL loans to treasury. That's all of the COVID EIDL loans that are in default.

Ms. VELAZQUEZ. For the record, isn't it true that the IG has cleared out that recommendation?

Ms. FROST. Yeah, there were a couple recommendations. I believe they're either cleared or will be cleared shortly.

Ms. VELAZQUEZ. As you are no doubt aware, there has been significant bipartisan concern around the SBA decision to award Funding Circle an SBLC license. Can you explain the SBA decision to continue to move forward with the award to Funding Circle, even after the CEO's announcement to sell its U.S. operations?

Ms. FROST. It was important to note that we had a strong, objective and career driven process to select the three new SBLC's. And that process actually had three phases. I'd like to walk through them quickly. The first was the due diligence committee, which were subject matter experts on my team who reviewed each and every loan.

Ms. VELAZQUEZ. Ms. Frost, can you talk to me about just Funding Circle? Because I have too many questions. I don't want to hear the story of the other two, but specifically the one that the CEO made the announcement to sell its operation in the U.S.

Ms. FROST. Absolutely. So all applicants went through the same process. But speaking specifically to Funding Circle, they were selected for a reason. They met SBA's requirements. They had a strong business plan that was going to help fill a market gap of small dollar loans across this country. And we are eager to work with Funding Circle to deliver on the promises in that application.

Ms. VELAZQUEZ. Okay. Yes or no? Did the company share its intention to sell its U.S. operation with the SBA prior to the award?

Ms. FROST. At the time of the award, we were not aware of that, no.

Ms. VELÁZQUEZ. You were not?

Ms. FROST. At the time of they were selected last fall, we were not aware.

Ms. VELÁZQUEZ. If Funding Circle had expressed that intention, would the SBA have considered that as part of their application?

Ms. FROST. You know, I don't know about a hypothetical scenario in which, you know, we would have had different information at the time.

Ms. VELÁZQUEZ. It is very real now.

Ms. FROST. Well, I can tell you at the time that they were selected, we were able to review full company financials, including audited financial statements, their management team, their experience, as well as their business plan.

Ms. VELÁZQUEZ. Yes or no? Now that the SBLC licenses have been granted, has the SBA had any discussion with Funding Circle about its decision to sell it is U.S. operation?

Ms. FROST. Yes. My team is regularly in contact with Funding Circle and the other SBLC's, including kind of regular oversight conversations, onboarding, conversations about technical capabilities, et cetera.

Ms. VELÁZQUEZ. Have you had any discussion with Funding Circle about its decision to sell its operation?

Ms. FROST. Yes, we have. My team reached out to them the night after their earnings call, when they made that public, and we have had several follow on discussions.

Ms. VELÁZQUEZ. Yes or no, has the SBA had any discussion with Funding Circle about its potential acquisition by a third party?

Ms. FROST. Yes.

Ms. VELÁZQUEZ. Am I correct in my understanding that the other licenses are currently available to be purchased or transferred?

Ms. FROST. Yes, they are. So there's, of course, 14 historic SBLC licenses. Those have traded hands through private sales for over 40 years. And SBA regularly conducts an overview of each and every change of control for an SBLC license.

Ms. VELÁZQUEZ. According to Funding Circle, the U.S. subsidiary is amply funded. Do you agree with that statement?

Ms. FROST. During their application, they showed that they were amply funded.

Ms. VELÁZQUEZ. When was the last time that the SBA examined capital levels?

Ms. FROST. So I know that we had to actually see money in the bank for them before they signed their 750 agreement, which was done about a month ago.

Ms. VELÁZQUEZ. A month ago. Funding circle also expected to start lending in April. Have they started making any loans?

Ms. FROST. They have not yet.

Ms. VELÁZQUEZ. Has Funding Circle signed a 750 agreement with the SBA?

Ms. FROST. They have signed, and we would like them to start making loans as soon as possible.

Ms. VELAZQUEZ. Does the SBA have any plans to award any additional licenses beyond the three that were just awarded?

Ms. FROST. We have awarded three at this time, and that is our plan.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman. I yield back.

Chairman WILLIAMS. Lady yields back. I now recognize Representative Mann from the great state of Kansas for 5 minutes.

Mr. MANN. Thank you, Mr. Chairman. Associate Administrator Frost, thank you for being here. Your engagement with this committee is important. I represent the Big First district of Kansas, which is 60 primarily rural counties in the western central, a little bit in the eastern part of our state. My district is home to more than 20,000 small businesses, and more than 80 percent of our employees in the Big First district are employed by small businesses, which help drive our economy and define the American dream. Unfortunately, I've heard time and time again from small business owners in the Big First who've been forced to shut their doors and end their livelihoods because of an aggressive, overly intrusive, and politically charged federal government. Specifically, I've personally met with one of several mom and pop firearm dealers in my district who the ATF forced to surrender their licenses and their way of life and stop contributing to their communities over minor cleric or clerical errors, like misspelling a name or using a county abbreviation in their documentation, which the President has declared zero tolerance for. I am concerned that parts of the federal government are being used as a bludgeon to stamp out small businesses that may or may not align with administration on a given political issue, especially with respect to brick and mortar gun stores on main street. This should not be a political issue. It is fundamentally un-American to crush small businesses simply because they do not agree with those in power on politics. A handful of questions. Are federally licensed firearm retailers eligible for SBA loans, and if so, which type of loans are they eligible for?

Ms. FROST. So, our loan programs at SBA support all types of small businesses across all different industries to include those who would sell firearms.

Mr. MANN. Does the SBA have any policy that applies additional eligibility requirements to federally licensed firearm retailers?

Ms. FROST. We do not. We have additional policy requirements on many different types of small businesses, for example, gas stations, but we do not have any on firearms firearm sales.

Mr. MANN. How many loans does the SBA have with federally licensed firearm retailers, and are they separately tracked, or how do you review, monitor, and oversee those loans?

Ms. FROST. So we track by NAICS industry code, but I don't know offhand, don't have the numbers in front of me in terms of how many, maybe two businesses that sell firearms.

Mr. MANN. Could you maybe get that for me through the NICS code? If you could get to my office, the number of SBA loans that exist with our mom and pop, our smaller, our small businesses that are federally licensed firearm dealers, that would be very helpful.

Ms. FROST. Happy to work with you on any agency requests.

Mr. MANN. And we can follow up on that. Are you aware of federally licensed firearm retailers being singled out in any way by the administration?

Ms. FROST. You know, I am laser focused on giving loans to American small businesses, and so that is what my office does and where my attention is.

Mr. MANN. Where have you seen loan growth while you've been in your position? In other words, what industries or segments have you seen that is growing, specifically in terms of new loans that are being generated?

Ms. FROST. Yes, we have seen tremendous growth in small dollar loans. So small dollar loans are up overall during the Biden Harris administration and looking this period of this year so far to last year, we're up about 25 percent in loans under $500,000 to all sorts of industries. Some of the core industries that our loans support would be things like restaurants and other mom and pop shops in downtowns across America.

Mr. MANN. Great. Thank you, Mr. Chairman. With that I yield back. And thank you again for being here this morning.

Chairman WILLIAMS. Gentlemen yields back. I now recognize and welcome back Mr. Representative Phillips from the great state of Minnesota.

Mr. PHILLIPS. Thank you, Mr. Chairman. And greetings, everybody. Ms. Frost, I recognize that about 85 percent or so of the EIDL and PPP loans that are subject to fraud were made under the last administration. So it is hard to hold all of you accountable for that. But I want to be prospective and ask where the $349 million that's been requested for fiscal year 2025 to support oversight, how specifically that will be used? As detailed as you can provide us.

Ms. FROST. Yes. There's two things I'd like to highlight about our budget request with regard to the kind of pandemic programs in the COVID EIDL portfolio. One would be for COVID EIDL servicing center, and that is to ensure that we have excellent customer service for the millions of Americans and small businesses who hold COVID EIDL loans, and that we're appropriately recouping that money through repayment and other collection activities. And the second thing I'd like to highlight is——

Mr. PHILLIPS. Can I ask? I want to hear the mechanics, the how, is it human? And one of my questions is AI. Is there any intention or interest in using artificial intelligence to do the work of perhaps thousands of people to actually assess these loans and identify which ones might be fraudulent?

Ms. FROST. Yeah, the rest of the—another portion of the budget request will go to the OIG to kind of track down these fraudsters. We actually, during the pandemic program under the Biden Harris administration, stood up a machine learning tool to help automatically screen all of the pandemic loans, including those done under the previous administration. And we used that really as a triage to help kind of best use our human led resources for human manual reviews.

Mr. PHILLIPS. And was that successful?

Ms. FROST. I believe it was very successful.

Mr. PHILLIPS. Okay, so any plans to further integrate such technology?

Ms. FROST. I will say there are lots of ideas. We do not have any concrete plans at this time.

Mr. PHILLIPS. Okay. Anyway, so back to the use of the 349 million.

Ms. FROST. Yeah. So the two things I'd like to highlight there would be the work of our COVID EIDL servicing center based in Fort Worth, Texas. And as I mentioned, also requesting additional support for the OIG so that they can go after these fraudsters. We have referred millions of loans to the office of the inspector general. They've got a big job, and they need some additional resources so that they're actually able to pursue the fraudsters and get this money back for the federal government.

Mr. PHILLIPS. Okay, appreciate that. A question about, you know, the decision that was then changed about the loans under $100,000, to pursue those. Can you just talk about how that decision was first made and why it was changed?

Ms. FROST. Yeah. So the decision was first made in early 2022 based on the best data and modeling available at that time. But actually, none of the portfolio had entered repayment. And so, we have updated that analysis now several times. And, you know, the longstanding policy of the agency has been to use all cost effective collection mechanisms to recoup the money from the COVID EIDL program on all sizes of loans. What changed is the analysis showed, based on updated data, wasn't previously available, that it would likely be cost effective to conduct that final step of collections of referring to Treasury. And so we have begun doing so.

Mr. PHILLIPS. And lastly, with your experience so far at SBA, if you could wave a magic wand and change anything that you've seen so far quickly, what would that be?

Ms. FROST. I would love better access to IRS tax data.

Mr. PHILLIPS. Okay, thank you. We'll get to work. With that I yield back, Mr. Chair.

Chairman WILLIAMS. Gentlemen yields back. I now recognize Representative Crane from the great state of Arizona for 5 minutes.

Mr. CRANE. Thank you, Mr. Chairman. Appreciate you being here. Ms. Frost. Ms. Frost, what is the SBA's number one form of capital generation?

Ms. FROST. You know, I believe that our loan programs are powerful tools to support American small businesses.

Mr. CRANE. I said capital generation. Do you guys generate any capital? Ms. Frost, where are you getting all this money that you are so excited here today to give out to American small businesses?

Ms. FROST. So, one of the incredible things about our loan programs is that they're subsidy neutral. It is one of the most impressive public private partnerships in America. And so, we partner with our loan, our loan, private sector lenders, and through fees and recoupment on our loan program, it actually operates at zero subsidy to the taxpayer. It is really an incredible partnership.

Mr. CRANE. So you guys don't have a product or a service that we don't know about at the SBA, that you guys are selling?

Ms. FROST. We——

Mr. CRANE. Little tchotchkes, hats, t shirts, anything like that?

Ms. FROST. No, we manage our loan programs under my office as well as the surety bond program.

Mr. CRANE. So is it fair to say, Ms. Frost, that you guys take money from the American taxpayer and then redistribute it to small businesses that you guys deem priority?

Ms. FROST. I don't think that's quite accurate. However, our direct disaster loan program does not operate at zero subsidy. That one is subsidized by the taxpayer to help small businesses across the country who've been impacted by devastating disasters.

Mr. CRANE. So you guys don't generate any money, right?

Ms. FROST. No, actually, the programs generate funding through fees and then recoupment on loans.

Mr. CRANE. Okay, Ms. Frost, what would you have to say to Americans that are paying their taxes, that fund these lending programs that aren't starting, small businesses that feel like they're being left out and they don't benefit at all from them?

Ms. FROST. I think that the entire economy and the entire country benefits from a vibrant small business economy. You know, if you are visiting restaurants, if your child goes to childcare, you know, if you kind of do recreational activities, you are benefiting from America's small businesses, and I am incredibly proud to support them.

Mr. CRANE. Yeah. Do you feel like they're benefiting from the inflation that the record high inflation that we're seeing right now, Ms. Frost?

Ms. FROST. I believe inflation's about 3 percent right now, and it is fallen significantly.

Mr. CRANE. Yeah. Okay. Ms. Frost, how much was the SBA defrauded during COVID?

Ms. FROST. The agency's best estimate on pandemic program fraud is $36 billion.

Mr. CRANE. $36 billion. I've heard the numbers are quite a bit higher than that, to the tune, there was about $200 billion worth of fraud.

Ms. FROST. So some confusion, there is, there's a difference between what we'd consider potential fraud and then likely fraud. And the way to best think about this is it is kind of like a metal detector, right? When you first walk through a metal detector and it goes off, you need to look into it a little further, but you don't actually know if it is something dangerous or if it is just a big belt buckle. So that potential fraud is like that metal detector going off. SBA found over $400 billion in potential fraud through our automated screening. That was the first of our four step process. Our second step was using data analytics, including that machine learning tool I just mentioned, to refine that fraud down or refine the potential fraud down so we could conduct manual reviews. That was our third step. We conducted millions of manual reviews on pandemic loan programs. And then the fourth step is referring that over to OIG. So you can think about it much like the metal detector. Maybe the metal detector's going off a lot, but you have to actually investigate each and every one to get a sense of what's real and what's just a big belt buckle.

Mr. CRANE. Okay, so your claim is $36 billion. Is that what you said?

Ms. FROST. That's the agency's best estimate, yes.

Mr. CRANE. Okay. Is there any chance that you guys will recoup any of that?

Ms. FROST. You know, so recoupment for fraud is done through the law enforcement community. That starts with the SBA, Office of the Inspector General. It includes the Secret Service, the Department of Justice, et cetera. And I know the President's budget requested additional funding for the SBA OIG for exactly that purpose, to go after the money.

Mr. CRANE. Ms. Frost, you said in your testimony, under the Biden Harris administration, there has never been a better time to start a small business. Is that correct?

Ms. FROST. That's correct.

Mr. CRANE. The Bureau of Labor Statistics reports that since Biden took office, we have $7 trillion added to national debt, 36 consecutive months of inflation above 3 percent, producer price index is 19 percent increase. Consumer price index, 19.4 percent increase. Credit card interest rates, 20.75 percent increase. Household debt for every American is $18,100 increase in taxpayer, and then 100 million working age people not participating in the workforce. Do you still stand by that statement?

Ms. FROST. I do. And I think that the data supports that. Americans across this country are starting businesses. The past three years have been the three highest business start years on record, and we have had over 17 million new business filings since the start of the Biden administration.

Mr. CRANE. Well, what about those statistics I just read you?

Ms. FROST. I think it is incredibly difficult to be a small business owner in America. And I admire each and every one of them for the tenacity that they have to continue working, regardless of the condition, to support their communities.

Mr. CRANE. Thank you, Ms. Frost. Thank you, Mr. Chairman. I yield back.

Chairman WILLIAMS. Gentlemen yields back. I now recognize Representative Pappas from the great state of New Hampshire for 5 minutes.

Okay, he's not here. All right. We now recognize Representative McGarvey from the great state of Kentucky for 5 minutes.

Mr. MCGARVEY. Thank you, Mr. Chairman. Thank you for being here, Ms. Frost. Like Ranking Member Velázquez and so many of my colleagues here today on this committee, I remain focused on increasing capital and access to capital for those who lack it, and ensuring that everyone does have that chance at the American dream of starting a business, of having it be successful. I'd like to spend some time today on the changes the SBA made to lending programs and its April 2023 rules on business lending. The finalized affiliation and lending criteria rule removed the concept of control of one entity over another as a basis for finding affiliation, arguing that the concept of control has proven particularly burdensome for applicants and lenders to understand and implement. As part of that change, the SBA stopped publishing its franchise directory. About a fifth of SBA lending goes to franchising, and SBA

Capital is an important source of startup funding for franchisees. So Associate Administrator Frost, now that the rule is final and the SBA no longer publishes the franchise directory, have you seen a change in the speed of approval for franchisee lending applications?

Ms. FROST. I would need to go check with the data to look specifically at the speed for franchisees, but I can tell you that the turn times in our loan processing centers are down. They're very quick right now, and I am very proud of the team.

Mr. MCGARVEY. Awesome. And has the SBA's decision to eliminate the directory led to, I should ask, what positive and negative changes have occurred as a result of the SBA's decision to stop publishing the franchisee directory?

Ms. FROST. I think our changes on the affiliation rules should be celebrated as a way that government has reduced unnecessary friction in our loan programs. You know, the concept of affiliation is this inherently governmental concept we developed for the SBA loan programs. And our lenders would constantly say, you know, they had to hire a team of lawyers to work through it. Now it is clear, it is based simply on ownership. Who owns the business and who does the business own? A business owner can understand it. Our lenders can understand it, and it is clear for everyone involved.

Mr. MCGARVEY. From serving as a legislator for a long time, I know that sometimes even the best intended policy has unintended consequences. Have you seen any unintended consequences from this change?

Ms. FROST. We have not at this time, no. Small dollar lending is up tremendously since last year, about 25 percent for loans under $500,000.

Mr. MCGARVEY. Thank you. Several of my colleagues and I have expressed concern to Administrator Guzman about the SBA's decision to award an SBLC license to Funding Circle. When she was before this committee in March, there were significant questions about Funding Circle's capital, adequacy, and performance prior to them obtaining the SBLC license. Are we setting a precedent where lenders with inadequate capital levels and significant losses can be let into that program?

Ms. FROST. I think it is important to note that in selecting the new three SBLC's, including Funding Circle, we reviewed full financial audited statements for each of the applicants to include Funding Circle, and they were appropriately capitalized. Now, every SBLC needs to meet our standards, and should there be any change in ownership or control for Funding Circle or any other SBLC, we review the kind of buyer, if you will, to ensure that they still met our standards. And we have conducted reviews like that as these previous licenses changed hand in the private markets over 40 times over the past few decades.

Mr. MCGARVEY. And as you guys have looked at this and what's happened, have there been any discussions about the SBA changing its metrics when considering applications for SBLC licenses going forward.

Ms. FROST. I believe we had a strong and objective process for selecting our SBLC's. Kind of had three phases. The first phase

was the due diligence committee, where subject matter experts on my team reviewed each and every application that came in, and they basically binned those applications as recommended for consideration or not recommended. Then it went to phase two, which was the review committee that included experts from around the agency to include legal, like our CFO's office, the Office of Investment, and we discussed and debated the recommendations of the due diligence committee. Right. You ask questions, you bring in other experience. And then finally, the third phase was the license committee vote. That was five career Members of our senior executive service, and they voted unanimously to select the three SBLC's that were selected last fall, which are Arkansas Capital Corporation, McKinley Alaska Growth Capital, and Funding Circle. And so that's kind of our process. I think it was a very strong, career led process, and I am proud of the team.

Mr. MCGARVEY. Thanks. And the last 30 seconds, just sort of an open ended question. What would you like to see from this committee that you would think help continue to grow small businesses in this country?

Ms. FROST. I think there's a lot that we can continue to do to improve our loan programs. We're regularly talking with our lenders and Members of your staff to do that. So some of the areas that we're excited to continue focusing on include what can we do for refinance capability within the 504 loan, and what can we do to improve line of credit products under our loan programs overall.

Mr. MCGARVEY. Thank you, Mr. Chairman. I yield back.

Chairman WILLIAMS. Gentlemen yields back. I now recognize Representative Davids from the great state of Kansas for 5 minutes.

Ms. DAVIDS. Thank you, Chairman. And thank you to you and the Ranking Member for holding this hearing today. And thank you to Associate Administrator Frost for being here to testify. Sorry I am short. I definitely appreciate the work that you and the folks at the Small Business Administration are doing to help our nation's entrepreneurs. You know, one of the top concerns we hear about from small businesses in our districts, and you've already heard it today, is access to capital. And I know your office is absolutely critical in ensuring that our main street businesses have the lending opportunities that they need to succeed. And with that in mind, I do want to touch on the Community Advantage Program.

And as folks know, this is a mission based lending program that was transitioned into the small business lending company program last year. In doing so, the SBA is attempting to support lenders that are better able to reach underserved entrepreneurs. That includes veterans, women, folks in rural areas, native owned small businesses. And this is with smaller dollar loans. So I am curious if you could tell me, to date, what progress have these mission based lenders made in improving access to capital for the underserved entrepreneurs that you all are trying to reach? And what kind of generally are SBA's goals for the community advantage lenders in the coming year or so?

Ms. FROST. Thank you for bringing up the Community Advantage Program. Mission based lending holds a special place in my heart, and I am proud of the that we did last year to create the

community advantage small business lending company license, where, as you mentioned, we brought 142 lenders onto that license so they can now conduct 7a lending that included 30 new mission oriented lenders last year. We have been clear that our top priority this year is getting those 142 lenders up and settled in the program. We developed a strong training. It was a 16 hours training, I believe, for each of them, and they have been working through it. I think we're either done or very nearly done with all of them on that. And community advantage lending is also up about 17 percent through quarter two of this year compared to the same time last year. We believe that the community advantage lenders are embracing the permanency of this license such that they're able to plan technology, recruitment and funding to better support these mission driven loans in the hardest to reach communities around the country.

Ms. DAVIDS. And then are there any aspects of that that you think that we probably need to know about as you move forward with continuing to implement and get the training going and that sort of thing, are there any issues that you are seeing yet or anything that we should be aware of as we plan?

Ms. FROST. I think that our smaller lenders and our mission based lenders face a lot of challenges, including kind of finding the business, bringing them in, as well as securing sources of funding for lending. So SBA is always interested in how we can support smaller lenders, and especially our community driven lenders in liquidity. So just having the money to conduct the loans, that's something that we're really interested in.

Ms. DAVIDS. Okay, thank you. And then I know in your testimony, you mentioned the SBA's revamped Lender Match tool, which includes the community advantage lenders. And the tool is important in connecting small businesses to SBA backed lending opportunities. But I do often hear from our kind of local small business owners and entrepreneurs that the SBA's tools and programs can seem daunting or complicated, which you actually kind of spoke to earlier. I am just curious how SBA has incorporated that feedback and has been reworking the Lender Match tool or other systems, if there are other systems that you've been reworking, to help those platforms specifically for access to capital work better?

Ms. FROST. So we relaunched Lender Match this past spring under the MySBA platform. Lender Match is an incredible tool. About 50,000 small businesses each month come into Lender Match looking for capital, and they can match with about 1,000 SBA lenders, including, as you mentioned, over, I believe, 250 or so community based lenders who can provide those loans. We kind of serve as the matchmaker through this process, and our relaunch this spring had tremendous improvements for our smaller lenders and our community driven lenders. Most notably, we went from what we'd consider a cold lead to a generated lead. So we ran all these small businesses through our risk mitigation framework to check for core elements of fraud and eligibility. Some of the big lenders could already do that sort of thing on their own, but now everybody gets that information, and we now have a 48 hour window for all of our lenders to look at the kind of leads coming in from these businesses and act on them. Previously, it was a kind of quickest

draw wins, or at least quickest draw gets an advantage, which, of course, would advantage larger lenders who were able to hire staff on that topic. Now, everyone has the same 48 hours window.

Ms. DAVIDS. Thank you. I appreciate that. We might follow up a little bit after this, but I yield back.

Chairman WILLIAMS. The lady yields back. And I now recognize Representative Meuser from the great state of Pennsylvania for 5 minutes.

Mr. MEUSER. Thank you very much, Mr. Chairman. Thank you, Ms. Frost. Appreciate you being here. So, there are some lenders who feel that they are inaccurately or inappropriately not receiving their funding for their guaranteed loans that they extended. As you and I had a conversation, and they feel as if they followed the four requirements which you outline and know extremely well. Confirm receipt of bar of certifications, confirm receipt of information that a bar was eligible, confirm the dollar amount, follow applicable BSA requirements. So, are you aware that there are lenders who feel they've fully complied with these four requirements, but are seeing denials?

Ms. FROST. So I am aware of these lenders, and I've actually had one on one or private conversations with many of them. But I think it is also important to note that SBA had clear underwriting standards for the PPP program. They were significantly less than the underwriting standards for our traditional 7a loan program, as it was an emergency program. But those underwriting standards were published in the IFR, the Interim Final Rule, in April of 2020, and stayed consistent. And we are ensuring that all of our lenders met those standards for underwriting before granting guarantee purchase.

Mr. MEUSER. But there are some that feel that the proverbial goalposts have moved and the documentation requirements have somewhat changed. Can you commit to honoring the guarantees made to lenders who complied with the requirements laid out in statute and regulation or in the FAQ's at the time the loan was made?

Ms. FROST. We will absolutely honor the guarantee for all lenders who met the requirements for the program.

Mr. MEUSER. Sure. Okay. So what is the timeframe for some of these disputes?

Ms. FROST. So when we're conducting a guarantee purchase review, it is depending on the risk rating of the file. It is a loan by loan review, and we request documentation from our lenders in many instances so that we can continue to move through the loan file. So we need to work in partnership with our lenders. They need to submit those documents to us in a timely fashion, and our team needs to review them quickly, and our team stands ready to conduct that work.

Mr. MEUSER. Work if we know of some very serious issues where some lenders may go out of business, or so they claim, can we make specific requests to you, and can you provide to them in detail what it is you need from them in order to properly assess their funding?

Ms. FROST. Absolutely. We have been consistent and clear about what meets the standards for underwriting for the PPP program in

our guarantee purchase review, and we will pass that information along to you and your team, as well as any lenders who are seeking it.

Mr. MEUSER. And can that be done within like a three to four week period if we were to submit that to you?

Ms. FROST. We can get that done quickly.

Mr. MEUSER. Okay, that's great. So, changing subjects. The CEO of Funding Circle, one of the three companies to be awarded a new SBLC license, reported two months ago that they basically couldn't handle it wasn't worth it, et cetera. The question is, is it common practice? And I assume it is not common practice, but why would the SBA approve an SBLC for a company with mounting losses and unwillingness to provide capital, as Funding Circle has disclosed?

Ms. FROST. So it is actually pretty common in the financial industry for businesses to take a loss for a couple years during, for example, a growth period, or at the start of a new loan fund program. So losses for a specific period is not in and alone itself considered a huge negative indicator. You do want to, of course, ensure that the company is properly capitalized, that they have appropriate loan loss reserves, and that they have prudent lending standards. Funding Circle did meet all of those requirements.

Mr. MEUSER. Okay. But it didn't work out for them very well.

Ms. FROST. I mean, I know that Funding Circle has expressed they may sell, but that may happen and it may not.

Mr. MEUSER. So we have had questions about Michigan registration initiatives in cooperation in partnership with the SBA. Do you feel, A, that that's appropriate, and B, are there taxpayer funds being utilized to register voters, specifically in areas that seem to benefit one party over another?

Ms. FROST. So I should be clear that I do not work specifically on this issue. But I understand from colleagues that this is simply providing information, much like a DMV, motor voter law, kind of just a link on our website.

Mr. MEUSER. Yeah, it is more than that. I mean, there's active engagement, there's kiosks, there's talk. There's certainly, even if it is a dollar, would you agree that even if it is $20 of taxpayer money, that is inappropriate?

Ms. FROST. Sir, as I mentioned, I don't work on this program. From what I understand, it is simply helping very, very busy small business owners get easy access to the state, kind of nonpartisan place to register to vote.

Mr. MEUSER. I am over my time. Thank you, Mr. Chairman. I yield back.

Chairman WILLIAMS. Gentlemen yields back. I now recognize Representative Scholten from the great state of Michigan for 5 minutes.

Ms. SCHOLTEN. Thank you so much, Mr. Chair. And thank you to Associate Administrator Frost for coming today. In your testimony, you discussed several ways in which the SBA, of course, is working to increase access to capital, something very important to me. My colleague, Mr. Meuser, and I just passed a great bill addressing this issue. In regards to establishing services such as the My SBA loan portal, how do these technologies assist small busi-

nesses who need more support, and are there improvements you are looking to make to these systems moving forward?

Ms. FROST. So the MySBA platform is an incredible kind of one stop shop or single entry point to SBA that will eventually cover all of our programs. We're kind of bringing them on, you know, as we're able. And so, for example, our disaster loan program is now on the unified lending platform under MySBA, this provides a modern, mobile first application for our customers so that small businesses are able to interact with the SBA using modern tools. They can do things like paying online, setting up recurring payments. They can make kind of some basic servicing actions, do that on their own in the app, and we have easy access to a messaging portal and our customer service center if they need a little more help.

Ms. SCHOLTEN. That's great. In your testimony, you also talk about significant progress that the SBA has made in making small dollar loans more available. However, you also note that half of the employer firms who applied for more capital didn't receive what they needed. Can you speak to any common issues that cuts across this group of firms and what prevented them from receiving the capital they requested? And are there areas in which the SBA can expand support to these businesses? What is it doing to address it, in other words?

Ms. FROST. Yeah, so the report that I mentioned where half of the businesses seeking funding did not receive it. To be clear, that wasn't just SBA loans. That was a Federal Reserve study, their employer firm study they do every year that looks at small businesses across America seeking access to credit through a number of different means. I actually think that the SBA loan products play a critical role in expanding access to credit overall in this country, and I want to make sure every business knows about them and our Lender Match tool as an easy way to get connected to SBA lenders.

Ms. SCHOLTEN. Making sure that small businesses know about the products that are available is also a passion of mine. We encounter numerous businesses all the time saying, you know, I didn't know about that. What are you doing to make sure that they're aware specifically about these products?

Ms. FROST. So my team works closely with several other teams at SBA who support getting the information out about SBA services and programs. That includes our field office. We have 68 field offices around the country, our Office of Entrepreneurial Development, who works in close partnership with resource partners around the country to reach America's small businesses and support them through SBA programs and through all other programs available to support small businesses.

Ms. SCHOLTEN. That's great. Lastly, I really appreciate the work that the SBA has done to prevent instances of fraud, including implementing new technologies to better provide screening and close collaboration with the Inspector General and other law enforcement agencies. It is also police week here on the Hill, and I wonder if you could tell us more about your work with law enforcement agencies to combat fraud. And are there ways that Congress can help support this work?

Ms. FROST. The way that our risk mitigation framework now works is that when the business submits information, we use a number of private sector and public databases, private sector, excuse me, and public, like government only sometimes databases, to check the information provided to validate it against these third party databases. Basically, to check that it is true and correct. We then are able to move those loans forward that are either if there's a hold, we're able to clear it, or we're able to say that there's no potential fraud concern. This is all done pre origination. And this risk mitigation tool was launched for our business loan programs for the first time ever last August. You know, traditionally, it was the lender's responsibility only to kind of prevent fraud. SBA thinks that we are stronger when we work together in partnership with our lenders, so they're going to keep doing their part. Now we're stepping up to do our part. And of course, anything that looks potentially fraudulent, or likely fraudulent, we refer to the office of the Inspector General. And the president's budget request did request additional funding for OIG so that they can go after the fraudsters, especially those who committed pandemic fraud.

Ms. SCHOLTEN. Thank you. I yield back.

Chairman WILLIAMS. Gentlelady yields back. I now recognize Representative Stauber from the great state of Minnesota for 5 minutes.

Mr. STAUBER. Thank you, Mr. Chair and Ranking Member Velázquez. Ms. Frost, we have a Minnesota business supporting 227 good paying jobs that has had a miserable and disappointing experience with the SBA's PPP audit and appeals process. The primary frustration with this process has been the lack of clarity and communication from the SBA throughout the entire process. Not only has the SBA failed to respond to two letters submitted by impacted organizations, but the SBA has also failed to respond to two elected officials from the state of Minnesota, Senators Klobuchar and Congressman Emmer, respectively. Ms. Frost, what is the SBA's procedure for following up on inquiries made by appealing parties?

Ms. FROST. So, we, of course, take all agency requests from Members of Congress and other elected officials seriously. You know, my office responds to them, and then, of course, it moves through an interagency concurrence process. So we work closely with our colleagues on any of those requests.

Mr. STAUBER. Okay, so the business requested a response. Senator Klobuchar requested a response, and so did Congressman ever. No response. Can you commit today you'll work with them?

Ms. FROST. Absolutely. Happy to work on any agency requests. And if you pass along the name of that small business, I will get it to my team so that we can look into it.

Mr. STAUBER. Thank you very much. Now, on to something. Another concern that I have with the SBA's procedures. Ms. Frost, when was the last time that you talked to Patrick Kelly?

Ms. FROST. I had lunch with Patrick a few months ago.

Mr. STAUBER. A few months ago? Explain. Two months ago? Three months? Do you remember?

Ms. FROST. I don't remember offhand.

Mr. STAUBER. A couple months ago?

Ms. FROST. Yeah. Maybe December or so.

Mr. STAUBER. Okay, December. Has Patrick Kelly spoken to you about any policy changes since he departed from the SBA?

Ms. FROST. You know, Patrick and I don't speak regularly, but when we had lunch, we talked primarily about our families. I have a young daughter, and he has two children.

Mr. STAUBER. So you didn't talk about any policy changes since he departed from the SBA?

Ms. FROST. We talked about some of the work that we had done together, but we primarily focused on personal matters.

Mr. STAUBER. Okay. Has Patrick Kelly spoken to you about Funding Circle in any capacity since he departed from the SBA?

Ms. FROST. No.

Mr. STAUBER. Do you know what Funding Circle is?

Ms. FROST. Yes, of course. Funding Circle is one of our new SBLC's.

Mr. STAUBER. One of the three new ones, correct?

Ms. FROST. That's correct.

Mr. STAUBER. That he lobbied for? Correct.

Ms. FROST. I am unaware of any contact between Patrick and Funding Circle, or any connection.

Mr. STAUBER. Has Patrick Kelly ever given you or any employee at the SBA either political or career, any instructions or advice relating to Funding Circle receiving an SBLC license?

Ms. FROST. No.

Mr. STAUBER. Not at all. Not at all?

Ms. FROST. No, not at all.

Mr. STAUBER. Are you aware of Patrick Kelly working with Funding Circle in any capacity?

Ms. FROST. I am unaware of any connection between Patrick and Funding Circle.

Mr. STAUBER. Are you aware of any type of consulting agreement that Funding Circle has with government forward where Mr. Kelly is currently employed?

Ms. FROST. I am unaware of any connection between Patrick and Funding Circle.

Mr. STAUBER. Per Funding Circle's own statements, it intends to sell its license, as it has intended to do since before the SBA officially awarded it. Since the agency continues to ignore Congress, today, I feel compelled to pass on a clear warning. If the license ends up in the hands of a former SBA employee, there will be an investigation into such a clear ethical violation. I hope we will not have to provide such oversight. And with that, Mr. Chair, I yield back.

Chairman WILLIAMS. Gentleman yields back. I now recognize Representative Gluesenkamp Perez from the great state of Washington for 5 minutes.

Ms. GLUESENKAMP PEREZ. Thank you, Mr. Chair. Associate Administrator Frost, thank you for being here today. As my colleagues have heard me share many times before in committee, before coming to Congress, I owned an auto repair and machine shop with my husband, and we utilized an SBA 504 loan to buy our shop. And that program was truly a vital source of capital for me, and I know it is for many other small businesses working in the

trades. I will say we did have a hell of a time going through the process. When Administrator Guzman was here in January, I asked her about what the agency was doing to make the experience more navigable for first time entrepreneurs who don't have a year to spend on the process. I am hoping you can provide an update on the agency's enhanced platform now that it is up and operational. How has it enhanced customer service? And how are you fielding a Representative sample of input from all sizes of businesses? Mom and pops up to the big guys, not just the folks that have a compliance department or administrators. And how would that feedback be incorporated?

Ms. FROST. Thank you for your question. I share your passion for making our programs accessible and easy to understand. And of course, the changes that we introduced last August, we believed really reduced some of these unnecessary frictions that made the program so complex, especially for first time folks come in to get a loan, or for anyone looking for those smaller dollar loans that, of course, often are underrepresented. Small businesses are first time startup businesses or businesses in the trades, rural businesses, et cetera. And so we're really proud of those reforms. We have seen small dollar lending respond, and we're up about 25 percent compared to the same time last year. Now, I think there's still more good work to be done on this and would be happy to work with you and your team on how we can further improve the loan programs.

Ms. GLUESENKAMP PEREZ. Are you aware of how applicants feedback might be incorporated or responded to, and how it is fielded? How is that feedback solicited?

Ms. FROST. So primarily for our business programs, our business loan programs, they work through private sector lenders, or for the 504 program through our CDC partners, our community development company partners. And so each and every one of them will have kind of different setups, different experiences on how they interact directly with the small business borrower. But we believe that setting the conditions for success will be kind of reducing those unnecessary frictions for the program. Right. If the lender can then better understand the program, they can better explain it to the small business. And of course, my team regularly works with lenders. We're actually now setting up the first ever small business lending advisory council that we can connect with the lenders directly. And importantly, on that advisory council, we are reserving seats for Members of the small business community to be there, as you are mentioning. Hopefully all sizes of small businesses can be represented so we can hear directly from them as well.

Ms. GLUESENKAMP PEREZ. Yeah, I would love the opportunity to engage on how those positions will be allocated, that it is not just like cute shops or big guys, that it is truly machine shops, auto shops, the kind of nuts and bolts of keeping our economy rolling. And thank you for your work. I am wondering if you could share how the updated tool will make it easier for borrowers to connect with lenders and compare rates for SBA backed loans. Any insight into how this might be helpful for rural entrepreneurs?

Ms. FROST. Yeah, so I think that Lender Match our tool to support our small business borrowers and connect them with SBA

lenders is incredibly important for our rural small businesses as I am sure you know, there are so many more banking deserts in this country about 1,700 last report that I saw, and that's especially true in the rural areas of this country. But now, anyone you know, you can, if you can access the Internet, you can go to Lender Match, you can put in some simple information about your business and the type of capital you need, and you are matched with up to, there's 1,000 participating lenders who can respond to that request. Some of the improvements we just made on this platform include bringing it under the MySBA platform. So again, that's our one stop shop. We're moving everything under that umbrella and also making it such that all of our lenders have the same 48 hours window before they're able to kind of click into support or opt in to a lead from a small business. That means from a small business perspective, and this is the most important perspective, after two days, I can log on and I can see all of the lenders who I've matched with, and I can select which lender I'd like to potentially get more information from and potentially get a loan from.

Ms. GLUESENKAMP PEREZ. Do you anticipate any particular impacts on rural communities access to capital through that?

Ms. FROST. I certainly anticipate that rural communities will use this tool, and I am excited to look into what we see and how the changes from the spring have hopefully impacted that program.

Ms. GLUESENKAMP PEREZ. Okay, thank you so much. I yield back.

Chairman WILLIAMS. Gentlelady yields back. And I now recognize Representative Maloy from the great state of Utah for 5 minutes.

Ms. MALOY. Thank you, Mr. Chairman. Hi. In preparation for this hearing, I reached out to some of the local chambers of commerce and regional banks in my district that spent a lot of time working with small businesses. And a lot of their mission is to try to get small businesses up and running and stable to help these economies in rural Utah. And when I reached out and asked about this hearing, I got a lot of complaints about the SBA, and I've grouped them into a couple of broad categories that I want to talk about.

So with the Chambers of Commerce, one in particular had an MOU with the SBA for trying to get SBDC assistants to a lot of the new and emerging small businesses. And they have gone through a lot of hurdles and hoops and made sure that people are registered with the right agencies, and they filled out the right paperwork, and then they're not getting a lot of funding. And so, it is been a frustrating experience for them that they were really enthusiastic about having this partnership and thought it was going to be really helpful and now they feel like it is a bureaucracy without a lot of benefit.

And then with the regional banks that specialize in lending to small businesses, they had a similar complaint. They feel like the SBA programs have a high cost of participation, a lot of bureaucracy, a lot of hurdles, and then not a lot of benefit in the end. And so they don't feel like they can recommend them to their customers. But then with things like EIDL loans, the SBA is directly competing with these same banks that are there and the communities,

trying to make sure that our main streets are vibrant. And then they're competing directly with a federal agency that's supposed to be helping and isn't really helpful. And so I am going to start with the banks. How does the SBA view its role in relation to private banks, especially considering direct lending initiatives that compete with private sector loans?

Ms. FROST. I believe that our business loan programs are one of the most incredible public private partnerships in this country, where we partner, we SBA partner with the private sector lender. They, of course, deliver the loan, and we provide a government guarantee on that loan. I know you mentioned some of the lenders you spoke with said the programs were cumbersome, a little clunky, and that's feedback we have been receiving for decades at SBA. We did take action on that last year to reduce some frictions, especially for smaller dollar loans. But I believe there's more work to be done on that as well.

Ms. MALOY. So what's the best way for lenders in Utah to give feedback to the SBA? Because they're right there on the ground. They're seeing what's not working. How do we get their feedback to you so that we can improve these programs?

Ms. FROST. Any lender who's interested in learning more about SBA loans, please send them my way to my team. We do have regularly quarterly calls on our key business loan programs where folks can submit questions, so lenders can submit direct questions. We have several different email addresses for each loan program where they can submit questions. And my team holds regular webinars providing information out to the lender community.

Ms. MALOY. Okay, I am going to have my staff follow up with you as soon as we're done here, because I think they would jump at this opportunity because they're really frustrated with how it is going. And then for the Chambers of Commerce, how does the SBA evaluate the effects, effectiveness of partnerships like this, where you have an MOU with an organization and you've got mutual goals, but the smaller entity, the rural Chamber of Commerce, or the local Chamber of Commerce doesn't feel like it is mutually beneficial anymore. The SBA is a large federal entity. It is hard to adjust. How are you evaluating how those partnerships work and adjusting so that they work for local chambers?

Ms. FROST. So I am not familiar with the particular MoU you are speaking about. And actually, the SBDC program is largely run out of the Office of Entrepreneurial Development. So a different office at SBA. I'd be happy to refer those questions over. But I can tell you I recently took a trip to Alaska to visit one of our new SBLC's, McKinley, Alaska growth capital. And there I also had the opportunity to visit some other lenders who support rural communities. They've got a lot of rural communities in Alaska, much like in Utah, as well as the rural communities and small businesses out there. And so, I do have some good firsthand perspective on how hard it can be to serve rural communities. And SBA is extremely interested in helping our capital programs better serve those small businesses.

Ms. MALOY. Well, from the people I represent, there's a lot of frustration that the potential is there for these to be really helpful, but the reality, it just isn't panning out. So I am going to have my

staff follow up with you. Let's see if we can get some of these things fixed. Thank you for your time with that, Mr. Chairman. I yield back.

Chairman WILLIAMS. Lady yields back. And now I recognize Representative Landsman from the great state of Ohio for 5 minutes.

Mr. LANDSMAN. Thank you, Mr. Chair. Thank you for your testimony and all your work today. I just have a few questions. I mean, you know, the paperwork issue is a big one, and I am glad you are working on it. I wonder if you, we have a little more time, if you could just talk a little bit more about what you have found to be the biggest barriers or the feedback that you get on these quarterly calls or wherever. In terms of just the bureaucracy around this, obviously we want to avoid fraud and we want to make sure the loans get to the right people. We also want to make sure that this is something that everyone can access, particularly those who don't have big staffs. Right. And so, I am curious about what you've heard and what in an ideal world, you would do to address those concerns. And then as part of that, what help do you need from this committee?

Ms. FROST. So, as I mentioned, we are kind of regularly engaged with the SBA lender community, where we both share information and receive input back from them. So just as an example, last week there was a lender conference here in Northern Virginia that I was able to attend, as were several Members of my team. This one was focused primarily on our 504 loan program, and we talked a lot about different restrictions around refinance opportunities in the 504 loan program, how we may be able to expand that. And that's something that my team is looking very closely at and plan to do in the near term.

I've also started something with my team where when we're launching a new product or we're moving forward with a new capability, we're doing our user acceptance testing with some of our smaller, often community based lenders. So, for example, I've mentioned several times during this hearing that we launched an update to Lender Match. We worked with some of our CA SBLCs to kind of try that before we did the full launch. Right, just to get their input. Similarly, we're working to modernize what's called 1502 reporting, which is our monthly report coming from the lenders on the status of their loan portfolio. And we have engaged with some of our smaller and community lenders to get their feedback on that product as we're finalizing the build around it.

Mr. LANDSMAN. Thank you very much. Can I just ask you about the unified lending platform? It seems to me that the technology, and I know this has come up already to better match potential borrowers with options, opportunities to do that with without a ton of staffing or paperwork, where you are simply making it easy using technology to help find some of these folks, but also when they search certain keywords, they find themselves on a platform, maybe the website, where they can very quickly get some questions answered and determine what opportunities there might be for them. Is that something that you envision the ULP doing, and where does this go? What's the next set of iterations, and what's that vision?

Ms. FROST. Thank you for that question. I think that Lender Match is an incredible tool to help our small businesses match. As you are mentioning, using technology. Very little kind of regular SBA resources are needed here to conduct these introductions between small businesses and lenders on an ongoing basis. I think some of the ideas that you are speaking about here certainly seem worthy of additional consideration about how can we use technology to better explain our programs in an understandable way, both for the lender community and especially for the small businesses, and would be happy to work with your team as we dive into those ideas.

Mr. LANDSMAN. We would love to work on this. I mean, I am on the VA committee and we're doing something similar with VA, which is to, you know, when a veteran goes and looks for something, something pops up that they're working through, which would just say, hey, we don't know if you are eligible for these things, but if you give us just basic service information, in this case, basic business information, we'll tell you very quickly what you might be eligible for. And that begins a conversation that doesn't exist at the moment. And so, if that is really an option, we'd love to work with you on that.

Ms. FROST. Absolutely. And I think that Lender Match does. It has a lot of those same components and same ideas. So a small business can come into Lender Match and say, here's some basic information about my business, and here's the sort of capital that I need. They submit that in. And then our lenders, the thousand or so lenders we work with through Lender Match, including about 250 community lenders, they each set up profiles and they say, this is the type of small business I want to work with, and these are the sorts of loans I provide. And together, then they get matched. I believe the data, and we'll look this up to make sure I've got it right, is that the average small business is matched with nine lenders.

Mr. LANDSMAN. Wow.

Ms. FROST. That's nine opportunities to kind of say, hey, maybe this is the right lender.

Mr. LANDSMAN. My time is up, and I want to be respectful of the Chairman. We'll follow up. Thank you very much. I yield back.

Chairman WILLIAMS. Gentlemen, yields back. I now would like to welcome and recognize Representative Malliotakis, good friend from the great state of New York, for 5 minutes.

Ms. MALLIOTAKIS. Thank you. Thank you, Mr. Chairman and Ranking Member, for allowing me to join the committee today. Ms. Frost. My constituent, Mr D'Andrea, runs an owner operated restaurant named the Roadhouse Restaurant. It is remained in the heart of my district in Staten Island for nearly 53 years. During the COVID pandemic, the Roadhouse Restaurant, like so many other small businesses across the country, ran into difficult financial times. With severe COVID restrictions in place by New York City, business slowed and Mr. D'Andrea looked to the SBA for a lifeline, and he now finds himself on the verge of financial ruin with his retirement. The equity of the building that the business resides under threat of foreclosure due to no fault of his own. But an admitted coding error, quote unquote coding error in the admin-

istration. Of the Restaurant Revitalization Fund by the SBA, Mr. D'Andre was granted $244,734 through the program on June 7th, 2021. Half of the initial grant, $123,857.69, was sent directly to the New York State Department of Taxation and Finance for payment of the Roadhouse's outstanding taxes. Now, Mr. D'Andrea was even given an assessment ID of the New York state taxes, taxes paid by the U.S. Department of Treasury. But on October 28th of 2021, the funds sent to the New York State Department of Taxation and Finance were returned to the Treasury because they lacked documentation and they had no idea what it was supposed to go to. They had no idea it had to go to the Roadhouse's accrued tax debt. So, since the return of these funds, Mr. D'Andrea's business has been assessed with additional taxes and penalties associated with the original tax debt of the state of New York. To date, these taxes and penalties are at a sum of $343,000.

Now, in February of 2022, my office engaged on behalf of my constituent, and in numerous letters and emails with the SBA, my staff was given excuses for missed deadlines for response. They were told that Mr. D'Andrea would receive the remaining funds in the following RRF disbursements, which never came to fruition. And then half of the award was improperly distributed to New York State due to the coding error, they admitted this. Mr. Chairman, I would like to submit the email correspondence for the record. Using the words of SBA staff themselves in November of 2022, they then looked into, "the circumstances surrounding Treasury's offset of part of the award to the Roadhouse Grill that occurred because of delinquent taxes owed by Mr. D'Andrea's company." And they said, "that should not have occurred in the RRF program, but for a coding error, we have no way of correcting that at this stage in the program." So how is it that we have Mr. D'Andrea received only half of the funds he was awarded. His debts are still unsatisfied with the New York State Department of Tax and Finance. The SBA admitted that half the funds were wrongly sent to New York State due to the, quote, "coding error." And now the SBA is threatening legal action on the full amount unless he perjures himself on the SBA portal and certifies that he received the $244,734, the complete amount, which he did not. So this is an error that the SBA—so I guess that's my first question to you.

Ms. FROST. So the Restaurant Revitalization Fund was, of course, one of our pandemic programs, and it helped thousands of restaurants across this country find their feet. Unfortunately, that program was oversubscribed, significantly oversubscribed. And so although it was a $30 billion program. SBA got that money out in record time with record small amounts of fraud.

Ms. MALLIOTAKIS. In this particular case, he was given the money, right? He was given half the money, but it was an error that it was sent to the state of New York and it was sent back to you, so you should have that money. The thing is, is that he should be given the money that he is entitled to. Do you agree?

Ms. FROST. As I mentioned, the program was oversubscribed, and so, unfortunately, we were not able to give funding to all of the eligible restaurants.

Ms. MALLIOTAKIS. He received the grant. He did receive the grant, right. He was part of the group that was eligible. And I

guess my question is, you know, this was an error on behalf of the SBA. They admitted to it. The money was there. They gave it to the state. The state returned it. I don't know what you guys did with it, but the fact is that he's owed this money, and now you are trying to penalize him even further if he doesn't sign this form, which would be a lie. He can't sign that form because he didn't receive the total amount that he was due. And so, I can understand that you don't have the specifics, perhaps, of my case and front of you, but I've been working for four years to try to resolve this issue. This is a small business that's going to go out of business. His whole retirement is going to lose everything if you guys don't work with us to address this.

Ms. FROST. So my heart goes out to the small businesses who are still struggling to recover from the pandemic. And I know that my team is prioritizing, ensuring that we are doing everything we can to support them. But the Restaurant Revitalization Fund in particular, is challenging because we were limited in the funds we were able to provide to eligible businesses.

Ms. MALLIOTAKIS. Okay, well, I hope to have your commitment to try to resolve this issue.

Ms. FROST. Happy to work with you and your team on that.

Ms. MALLIOTAKIS. Thank you very much.

Chairman WILLIAMS. Lady yields back. And I now like to thank our witnesses for your testimony, Ms. Frost, and appearing before us today. Without objection, Members have five legislative days to submit additional materials and written questions for the witnesses to the Chair, which will be forwarded to the witness. I ask the witness to please respond promptly if there's no further business with abject and the committee is adjourned.

[Whereupon, at 11:24 a.m., the committee was adjourned.]

APPENDIX

Statement of Kathryn Frost
Associate Administrator, Office of Capital Access
U.S. Small Business Administration

Good morning, Chairman Williams, Ranking Member Velazquez, and members of the committee. On behalf of our Administrator, Isabella Casillas Guzman, and the entire Agency, thank you for the strong Congressional support of the Agency's lending programs and I appreciate the opportunity to appear before you today.

I serve as the Associate Administrator for the Office of Capital Access (OCA) where I am responsible for the Office of Capital Access's administration of SBA's 7(a) business loans, the 504 Loan Program, the Surety Bond Program, the Microloan Program, and SBA's Disaster Loan program—as well as the Agency's Paycheck Protection Program, COVID Economic Injury Disaster Loan (COVID-19 EIDL) program, and Restaurant Revitalization Fund. Collectively, these programs connect creditworthy small business entrepreneurs to capital when they otherwise are unable to obtain conventional sources of capital. Our business loan programs work in partnership with private sector lenders to lend necessary capital to start or grow small businesses. SBA loans were behind companies and products that are now household names, like Ben & Jerry's Ice Cream, South by Southwest, and Boppy Pillow.

Under the Biden-Harris Administration, there has never been a better time to start a small business. Since 2021, we have experienced a Small Business Boom, with over 17 million Americans filing new business applications. Starting a new business is an "act of hope" as President Biden says, and the record numbers of Americans starting a small business shows the optimism Americans have about the future of our economy. At SBA, we are working each day to ensure that every American who wants to start a small business can pursue their dream of entrepreneurship.

Women and people of color are leading the Small Business Boom. Our Nation has seen the fastest creation rate of Hispanic-owned businesses in more than a decade — over 20% faster than pre-pandemic levels. SBA data shows that lending to Latino-owned businesses is up more than 80% since the start of the Biden-Harris Administration. Similarly, Black-owned businesses are growing at the fastest rate in more than 30 years. SBA data shows the number and share of SBA-backed 7(a) and 504 loans going to Black-Owned Businesses more than doubled since 2020. Additionally, women continue to start businesses at higher rates than their male counterparts, and in 2023, women in the United States opened as many as 1,200 new establishments a day.

Whether a business is newly created or already established, it needs access to affordable and patient capital so that it can grow and create jobs in the community. SBA works with private sector lenders to provide government-guaranteed loans to qualified borrowers with the agency sharing in the risk so that lenders can put more capital to work.

SBA has invested in modern technology like the Unified Lending Platform (ULP) so that we can help borrowers get a loan decision more quickly. We also unveiled an updated LenderMatch tool to connect borrowers to financial institutions so that borrowers can compare

rates from multiple lenders offering SBA-backed loans. Our technology reforms now also include an eligibility screening at loan origination that protects taxpayer dollars by ensuring that a loan applicant is evaluated for prior fraud activity before the loan is disbursed, which also gives lenders additional assurance that a loan meets the requirements to receive a government guarantee.

These reforms are making a difference. In 2023, SBA delivered more than $50 billion across our capital, investment and disaster programs. Specifically, that includes $27.5 billion in 7(a) loans to more than 57,000 small businesses across the Nation. Additionally, SBA approved $6.4 billion in 504 loans to nearly 6,000 borrowers last year.

One of the persistent problems for small businesses has been the availability of small dollar lending. Small SBA loans fell significantly during the previous Administration, with 7(a) loans under $500,000 falling 40% from 52,000 in FY2016 to 31,000 in FY2020, and 7(a) loans under $150,000 falling 42%, from 38,000 in FY2016 to 20,000 in FY2020. When businesses cannot access small-dollar capital, there are significant consequences such as the inability to meet employee payroll expenses with particularly significant harm for underserved communities – including minority populations, women, veterans, and rural Americans.

Reversing this decline has been one of Administrator Guzman's top priorities. In 2022, she expanded the Community Advantage loan program and proposed two rules aimed at increasing small-dollar lending by expanding lender participation and making it easier to do business with the Agency.

In August of last year, those rules became effective. Underwriting requirements for loans under $500,000 were simplified and closely align with industry standards to ensure an SBA loan is a competitive offering. Also, as a result of these rules, complex affiliation tests are no longer a barrier to eligibility; and mission-driven lenders now have permanent status through the new Community Advantage SBLC license, resulting in **30** newly enrolled lenders. At the same time, SBA also established the most robust front-end fraud control system ever in the program, a change strongly supported by the Inspector General.

We now have 9 months of performance data after the implementation of these reforms, and I'm pleased to report on behalf of Administrator Guzman: the rules are working. In FY2024 to date, SBA has approved more than 22,000 7(a) loans under $150,000. That puts us on pace to nearly double the number of small loans approved in the final year of the previous administration. It's also a 30% increase compared to this time last year. That's 1,500 more businesses getting approved for a small loan every month than just a few years ago. Moreover, many of these businesses are among market gap populations, including women, minority entrepreneurs, employees purchasing a portion of a business from its owner(s), and startup small businesses. For this progress, we give credit to our partners in the lending community, who have embraced the new opportunity and seized it to deliver more capital to small businesses.

Despite notable progress, there are still gaps in the availability of small-dollar loans. The Federal Reserve's 2024 Report on Employer Firms showed half of employer firms who sought capital did not receive what they needed. That's why SBA is pressing ahead with additional

reforms. SBA has enrolled three new private sector lenders through the SBLC program to increase the supply of capital, each of which demonstrated through the license application process a commitment to filling a particular market gap.

We're also moving to expand the pool of eligible, creditworthy small business borrowers. In April, our nation celebrated Second Chance Month to highlight ways that we can help justice impacted individuals reenter society. One of the best ways to reduce the risk of recidivism is to provide stable employment which, for those with convictions, often is entrepreneurship. Individuals who have prior convictions are currently eligible for most SBA programs, but asking questions about criminal history often creates a chilling effect that deters people from applying even if they would qualify.

SBA is committed to breaking down barriers that limit access to our programs and we have announced an initiative to "Ban the Box" by removing irrelevant criminal history questions on loan applications. The SBA rule change also will improve pathways to entrepreneurship for formerly incarcerated individuals by eliminating SBA capital program restrictions on Americans who have completed their sentences for past crimes, including Americans on parole and probation. Under SBA programs, lenders will continue to conduct individualized reviews that address fraud risks and assess the creditworthiness of borrowers.

The President's 2025 Budget Justification includes legislative language to enable SBA to deliver on the Small Business Act's longstanding directive of directly lending to creditworthy small businesses unable to secure credit in the private sector. Specifically, the President's Budget proposes added flexibility for SBA's direct lending terms, to enable the agency to make fair, competitively priced direct loans to businesses, at no additional cost to the taxpayer.

SBA has extensive experience with direct lending in our disaster lending program, including successfully lending $2.98 billion to 43,108 borrowers in FY2023. SBA is currently active in more than 348 areas across the country with disaster declarations, including the Francis Scott Key Bridge collapse in Baltimore.

Finally, as Administrator Guzman testified in March, SBA is in a better position than we ever have been to combat fraud, waste and abuse. SBA's investments in technology including our new Risk Mitigation Framework ensures that every SBA loan is screened for fraud prior to disbursement. SBA has implemented GAO recommendations to improve SBA's fraud prevention measures, and we work closely with the Inspector General and other law enforcement agencies to refer suspected fraud for investigation and prosecution.

I know there are many other issues that you would like to discuss, and I look forward to your questions. Thank you for the opportunity to appear before the Committee today.

House Committee on Small Business
Questions for the Record
"Under the Microscope: Reviewing Key SBA Programs with Associate Administrator Frost"
Hearing held on May 15, 2024
Witness: ***Associate Administrator Frost***

Questions from Rep. Roger Williams (R-TX-25), Chairman

PPP:

1. Is the SBA running out of funds to service PPP loans?

Yes, SBA is running out of funds for servicing PPP loans. SBA sent a letter to Congress highlighting this issue on September 28, 2023. Absent the funding requested in the 2025 Budget, SBA will have insufficient resources for processing critical transactions and audit work under Paycheck Protection Program (PPP), Restaurant Revitalization Fund (RRF), and Shuttered Venues Operating Grant (SVOG).

2. Have you or any other SBA employees had conversations with lenders about charging lenders fees on PPP loans? If yes, why?

Yes, Office of Capital Access (OCA) officials had conversations with several lenders during March and April, 2024 who held some of the largest remaining volume of PPP loans in their portfolios.

3. What fee authority is the SBA relying on to charge a PPP fee?

SBA has not charged an annual or ongoing fee to lenders. SBA has authority to charge fees by Office of Credit Risk Management (OCRM) given the remaining cost of overseeing these lenders.

4. Are you aware that the fees charged on standard 7(a) loans were expressly waived by Congress for the life of any PPP loan ever made?

Yes, for PPP loans, the CARES Act waived the upfront guaranty fee and the lender's ongoing fee in secs. 7(a)(18) and 7(a)(23) of the Small Business Act. See 15 USC 636(a)(36)(H). The CARES Act also waived the prepayment penalty in 15 USC 636(a)(36)(R). There was no waiver of lender oversight fees.

5. Are you aware that oversight fees cannot be charged on activities that are not associated with OCRM's direct oversight activities of an SBA lender?

Yes.

6. Are you aware that the Federal Credit Reform Act of 1990 requires that any fees collected pay for the costs of the loan itself, and any administrative costs, like the SBA servicing a loan portfolio, must be a separate line item?

Yes.

7. A consultant hired by the SBA informed the SBA that Treasury was more successful in collecting on smaller loans. Nearly 90% of PPP Loans that SBA ended collection on were valued at $25,000 or less. Given this, why did the SBA not work with Treasury sooner to address these debts?

SBA has always collected on every PPP loan. SBA made a data-driven decision to pursue collection on small PPP loans in-house without referring loans to Treasury when it concluded through an analysis that referral to Treasury would not be cost effective. When SBA updated its analysis of PPP data and concluded that it would be cost effective to refer small PPP loans to Treasury, SBA began immediately working with Treasury for the orderly referral of these loans.

8. The SBA made a serious error in failing to take collection action on PPP loans valued at under $100,000 and by automating its PPP forgiveness. Now the SBA must try to collect on these loans. How does the SBA plan to restart collection on these PPP loans?

Please see the answer above. SBA has always collected on every PPP loan. SBA will continue all collection activity, including phone calls, emails, messages, and letter outreach to delinquent PPP borrowers. As stated previously, SBA is working with Treasury to address delinquent debts and the Agency's policy is to send all delinquent debts, including PPP debts, to Treasury when they are 120 days delinquent.

Direct Lending:

9. You said that the SBA will set up a direct lending program "if given the tools to do so." What are the tools that the SBA believes it would need to set up a direct lending program?

The President's Budget requests legislation from Congress to allow SBA to charge an interest rate that allows a direct lending program to operate at zero subsidy.

10. Does the SBA envision using Lender Match to launch a new direct lending program?

Lender Match is a tool to connect borrowers to private sector capital that first launched more than 10 years ago—around 50,000 users search for funding through Lender Match each month. SBA briefed the Committee about Lender Match on February 27, 2024, on improvements launched this past Spring. Lender Match is not connected to the President's FY25 Budget proposal on direct lending.

11. With the SBA's plan to grow its lending portfolio through the new direct lending program, why has the SBA decided to be in the business of competing with the private sector?

By statute, SBA's authority to make direct 7(a) loans only extends to businesses that are not able to obtain an SBA-guaranteed loan. In accordance with the President's FY 2025 Budget Proposal, a direct 7(a) loan program would further enable SBA to address gaps in access to small dollar lending that SBA 7(a) lenders are currently unable to fill.

12. What prudent lending requirements are being lowered as part of this direct lending proposal? Follow up: Why does the SBA support different lending standards for prospective borrowers of government-guaranteed loans?

There would be no difference in prudent lending requirements for an SBA direct loan program.

13. The SBA requested a maximum interest rate increase on direct loan borrowers in the FY25 President's budget request to execute the agency's proposed new direct loan program. How is the SBA planning to get the capital to make a direct loan on day one? Follow up: Are any losses going to be mixed in with the 7(a) program?

The President's Budget requests legislation from Congress to allow SBA to charge an interest rate that enables the agency to structure the direct 7(a) loan program to operate at zero subsidy

14. Follow up: Do you expect the borrowers of the 7(a) program to cover the costs of a high-loss direct loan program?

SBA is committed to expanding access to capital for America's small businesses and entrepreneurs. The SBA Administrator testified that SBA would structure the direct 7(a) loan program to be cost-neutral. Direct lending can help to fill gaps for access to smaller dollar lending, especially for historically underserved communities. A recent study published in the National Bureau of Economic Research found that SBA direct disaster loans "reduce exit and bankruptcy, increase employment and revenue, unlock private credit, and reduce delinquency." The study, After the Storm: How Emergency Liquidity Helps Small Businesses Following Natural Disasters, also found that SBA direct disaster loans have a crowding-in effect of private credit but did not find capital reallocation away from neighboring firms but rather more evidence of positive spillovers on local entry. Providing direct 7(a) loans could have similar positive effects by helping businesses start a path to becoming qualified borrowers for SBA-guaranteed or conventional bank loans in the future.

15. When the Administrator testified on the Hill last month, she made it clear that it would take an act of Congress to set up a direct lending program. Will you and the SBA commit to not taking any actions to skirt this statutory check on the S-B-A's ability to set up this program in the future?

As part of the FY 2025 Budget proposal, the Administrator testified that the Agency has requested Congressional support to begin direct lending.

16. The SBA's 7(a) rule changes finalized last year were meant to make lending for non-SBA lenders quicker to more small businesses, but the President's budget proposes a new direct lending program. Given that COVID EIDL lost the taxpayers hundreds of billions of dollars in fraud, why should we trust the SBA with more lending responsibilities?

SBA has been making direct disaster loans since the Agency's inception in 1953 and has an impressive track record of eliminating and reducing fraud so that only eligible homeowners, renters, businesses and nonprofits are able to obtain disaster loan assistance.
SBA's long-standing controls to determine loan eligibility and mitigate fraud were stripped away from the COVID-19 EIDL program by the CARES Act. During the first 9 months of the COVID-19 EIDL program, SBA was required by the CARES Act to accept self-certification and prohibited from obtaining IRS tax records from the applicant when determining eligibility. Under the Biden-Harris Administration and Administrator Guzman, SBA put in place basic fraud controls like pre-approval screening, checking tax returns obtained from the applicant, and checking Treasury's Do Not Pay database.

17. Is there guidance on how the SBA regulates the basic concepts of KYC and BSA to all of its SBA Supervised Lenders? Follow up: How do you regulate that compliance?

SBA's review activities establish an understanding of the BSA/AML Program and aligning policy and procedures that are developed and operationalized by identified lenders based upon the expectations established by the Financial Crimes Enforcement Network (FinCEN) and meeting data gathering and verification obligations for Customer Identification Program (CIP) and Beneficial Ownership (BO) requirements. Review activities included a review of BSA/AML Program structure and documents (e.g., policies, procedures, and supplementary forms) to assess CIP and BO compliance.

Targeted Risk-Based Reviews have been used to assess compliance.

SBLCs:

18. SBA admitted three new Small Business Lending Companies (SBLCs) into the 7(a) program this past November. Follow up: Could you provide an update on the performance of the three new SBLCs and how many loans they have made to date?

FY 24 year-to-date performance for the three new licensees is as follows: (a) Alaska Capital Growth: 7 loans for $10.23 million; (b) Arkansas Capital Corp: 5 loans for $1.09 million; and (c) FC SBA Lending LLC: 0 loans. FC SBA Lending LLC voluntarily surrendered its SBLC license effective June 24, 2024.

Since receiving their SBLC licenses, the performance of the two new SBLCs has been satisfactory. Prior to the execution of their Form 750 to participate as SBLCs, these two lenders were participating in the 7(a) program as non-federally regulated lenders.

19. Do you have any plans to admit additional SBLCs? If so, when is the next planned open SBLC application process?

On July 22, 2024, SBA announced that we planned to reopen the SBLC application process as part of the Green Lending Initiative with the goal of awarding 3 new SBLC licensees.

20. What conditions or factors would lead you to consider admitting additional SBLCs into the 7(a) program?

During the rulemaking to repeal the 1982 moratorium that capped SBLC licenses at only 14, SBA stated our intent to fill market gaps for small businesses, including low-dollar lending. Filling gaps in the marketplace to ensure our small businesses can access the capital they need remains our priority.

21. The SBLC application review usually takes about a year to complete. The SBA's most recent SBLC application period only took 3 months to complete. Why did the SBA expedite this process to such an extreme? Follow up: Who made the decision to expedite the process?

The SBA had not awarded new licenses for SBLCs in more than 40 years; and SBA established a new process to ensure selection of strong SBLCs. The details on the 2023 SBLC Application process were announced in the Federal Register in May 2023 and the Agency announced SBLC selectees in October 2023; the licenses were finalized in February and April 2024. SBA has modern technology that can make the review, selection, and onboarding process quicker than it would have been in 1982 when the moratorium began.

22. Why did the SBA decide to move the SBLC application review process from the Office of Credit Risk Management to the Office of Financial Programs Operations for the first time ever for the three latest SBLC licenses? Follow up: Yes or no—the role of the Office of Credit Risk Management is tasked with conducting risk-based analyses of SBA's lending partners, correct?

The SBA had not awarded new licenses for SBLCs in more than 40 years; and SBA established a new process to ensure selection of strong SBLCs.

SBA's Office of Financial Assistance (OFA), not Office of Credit Risk Management (OCRM), conducts the analysis of SBLC applications when an SBLC license changes hands. However, given the small staff

in the department and the heavy workload involved with reviewing three new SBLC applications in addition to their full-time responsibilities, OCA made a sound, responsible decision to leverage its extensively experienced finance professionals from other offices and created a Due Diligence Committee (DDC) to provide the initial review of the applications. The DDC was comprised of 6 career employees: 3 from the Office of Financial Program Operations (OFPO), 2 from OFA, and 1 from OCRM. The results of the DDCs' initial review were then presented to the Review Committee which was comprised of the License Committee as well as other leaders from within SBA including the Office of Capital Access (OCA), Office of General Counsel (OGC), Office of the Chief Financial Officer (OCFO), Office of Investment and Innovation (OII), Office of Veterans Business Development (OVBD), Office of Women's Business Ownership (OWBO), and the front office who asked questions, and provided additional perspective on potential SBLCs to the Licensing Committee for final decision.

23. Yes or no—the role of the Office of Financial Programs Operations is to originate, service, and liquidate 7(a) and other business loans in processing centers across the country, correct?

The Office of Financial Programs Operations' (OFPO) mission is to lead the financial services industry through quality products and services to our partners and customers, and to protect the integrity of SBA loan programs. OFPO responsibilities include originating, servicing, and liquidating all OCA loan products as well as processing guaranty purchase requests on 7(a) loan guaranties. OFPO 7(a) Loan Guaranty Processing Center (LGPC) reviews 7(a) loan guaranties for both seasoned 7(a) lenders who choose to send certain transactions to the Center and new 7(a) lenders who do not yet have delegated authority. This would include lenders who are new SBLCs and Community Advantage lenders (prior to and since becoming CA SBLCs) who are (were) seeking 7(a) delegated authority, which make it uniquely equipped to be involved in the process for new SBLC applicants. OCA leveraged all three of these skilled departments, OFPO, OFA, and OCRM, in the review and on-boarding of the new SBLCs.

24. Follow up: Can you explain how the Office of Financial Programs Operations is more appropriate than the Office of Credit Risk Management to analyze the financials and application of a prospective SBLC when that is not their function?

All three of these OCA departments - OFA, OFPO and OCRM - have finance professionals with extensive private sector and government lending experience and financial analysis training and were leveraged during this end-to-end process.

25. Has any political appointee at the SBA ever made the decision to move the SBLC application process to an office that has never performed the review of SBLCs before?

For the first time in 40 years, SBA lifted the moratorium on the number of SBLC licenses to promote responsible small business lending through non-depository lenders backed by SBA loan guarantees and improve access to capital for small businesses across the country. In order to effectively enact this rule change, OCA created a Due Diligence Committee (DDC) to provide the initial review of the applications. The DDC was comprised of 6 career employees: 3 from the Office of Financial Program Operations (OFPO), 2 from the Office of Financial Assistance, and 1 from the Office of Credit Risk Management. The results of the DDCs' initial review were then presented to the Review Committee which was comprised of the License Committee as well as other leaders from within SBA including OCA, OGC, CFO, OII, OCFO, OVBD, OWBO, and the front office who asked questions, and provided additional perspective on potential SBLCs to the Licensing Committee for final decision.
OCRM continues to supervise all SBLCs.

The SBLC application process and applicant requirements are outlined in 88 FR 32623. The application process for an SBLC change of ownership or control is stated in 13 CFR 120.466. The process is broken into two phases: (a) the Lender Assessment Plan (requirements detailed in SBA Form 2498); and (b) the Application (requirements detailed in SBA Form 2499). SBA's application evaluation process is described in 13 CFR 120.467. Change of control requirements are described in 13 CFR 120.468.

26. According to federal regulations, each applicant who receives notice from the SBA that it may proceed to the final review must submit a complete application to the SBA within 90 calendar days. Did all three of the new SBLCs do this? OCRM

Yes.

27. How many times has a company with net operating losses been approved for an SBLC license over the entirety of the program?

The SBA had not awarded new licenses for SBLCs in more than 40 years; and SBA established a new process to ensure selection of strong SBLCs. SBA does not have accessible records on financial information of the original SBLCs at the time of their original approval.

For SBLC transfers of control or ownership, it is common for a change of control applicant to present a business plan that projects operating losses for the first several (2-4) years until the licensee's SBA loan portfolio reaches a size and annual origination volume that is self-sustaining.

28. How many times has an SBLC applicant been approved for an SBLC license when it was communicating at the time of application that it did not intend to retain the license under their ownership?

As stated above, SBA had not approved new licenses in more than 40 years, and we are not aware of any case where SBA approved a transfer of control or ownership of an SBLC license to an entity whose business plan contemplated a near-term (i.e. less than 12-24 month) sale of the SBLC license.

29. How many times has the SBA taken any formal or informal enforcement action with an existing SBLC in the event that it was showing a net operating loss during the time of having a license?

During the last five years, SBA took one Informal Enforcement Action against an SBLC that was due in part to the SBLC experiencing a net operating loss that adversely affected its capital. The Lender was able to correct the deficiency and the Informal Enforcement Action was terminated.

30. How did your office respond to Funding Circle's comments that it didn't believe that the capital and cash required for the SBA loan portfolio "was the best course of action" and that they had "received indications of interest for the U.S. business?"

Associate Administrator Frost testified in the hearing that SBA spoke to Funding Circle after their public earnings call in which they stated their interest in selling their US-operations.

31. At the time of the SBLC initial award on October 31, 2023, you said that the SBA was not aware of Funding Circle's intention to sell its SBLC license. But you confirmed that the SBA became aware of this intention a month before the 750 agreement was signed between Funding Circle and the Agency. Please explain the SBA's decision move forward with awarding a final SBLC license to Funding Circle, even after the announcement to sell its U.S. operations.

Changes in parent ownership are common among both SBLCs and banks. Last year, of the 86 banks that either merged with or were acquired by another bank, some were active SBA lenders prior to the transaction and continued to be afterwards. For example, Montreal-based BMO purchased Bank of the West, and Old National purchased CapStar. The founders of Velocity SBA, an existing SBLC lender, sold a majority of their interest to the Cranemere Group Limited, a UK-based financial services company. Prior to approval, this transaction was carefully vetted and analyzed by SBA to ensure adequate program oversight and protect American taxpayer dollars. Funding Circle's SBLC— FC SBA Lending LLC—was selected from a competitive field of applicants because of their demonstrated ability to successfully meet SBA lending standards and requirements, lend to credit-worthy small businesses, and fill market gaps in SBA lending.

The SBLC application process and applicant requirements are outlined in 88 FR 32623. The application process for an SBLC change of ownership or control is stated in 13 CFR 120.466. The process is broken into two phases: (a) the Lender Assessment Plan (requirements detailed in SBA Form 2498); and (b) the Application (requirements detailed in SBA Form 2499). SBA's application evaluation process is described in 13 CFR 120.467. Change of control requirements are described in 13 CFR 120.468.

Effective June 24, 2024, Funding Circle voluntarily surrendered its SBLC license.

32. Did the Administrator ever instruct you or any career employees at the SBA to approve the SBLC license for Funding Circle? Follow up: Did you ever instruct any career employees at the SBA to approve the SBLC license for Funding Circle?

As testified at the hearing, the selection process for the first new SBLC licenses in more than 40 years was strong and objective. Career senior executives voted on the selectees, and none were instructed on how to vote. Please refer to SBA's letter to the Committee of May 14, 2024.

Effective June 24, 2024, Funding Circle voluntarily surrendered its SBLC license.

33. Do you believe changes are needed to the SBLC approval process to avoid situations where a company immediately seeks to sell its SBLC license?

The intent of awarding new SBLC license is for the awardees to use them to lend to small businesses, as they lay out in their applications. When SBA reopens the SBLC application, the Agency is considering restricting any new awardees from selling the license for a period of time. On June 24, 2024, Funding Circle sold their entire US operations to iBusiness Funding LLC, a division of Ready Capital Corporation. Ready Capital Corporation is the ultimate parent, which is a publicly-traded entity. The SBLC license is held by ReadyCap Lending LLC, which is owned by ReadyCap Holdings LLC, which is in turn owned by Ready Capital Corporation. iBusiness Funding LLC, which bought FC USA, is an affiliate of ReadyCap Lending LLC.

34. Of the three new SBLC licenses, only Funding Circle has experienced a delay in making 7(a) loans. As of your testimony, they have made no 7(a) loans. What was the reason for the delay?

Funding Circle was eligible to make SBA 7(a) loans, and SBA anticipated that Funding Circle would make loans and fulfill their stated business plan. Funding Circle did not make any loans prior to the voluntary surrender of their SBLC license on June 24, 2024.

Community Advantage:

35. Because CA SBLCs exist only in regulations, and not in statute, can you explain why the SBA believes that CA SBLCs are permanent?

CA SBLCs have been enrolled in the existing SBLC program which provides lenders with more certainty and a pathway for growth. CA SBLCs had previously participated as lenders in SBA's Community Advantage Pilot Program. The nature of pilot programs is that they are temporary and are subject to being terminated. As pilot program lenders, the lenders could not be certain that the program would be renewed beyond any 2 to 3 year period. Therefore, pilot lenders were reluctant to invest in staffing up, training, and building out infrastructure to fully participate in the program. As CA SBLCs, the lenders have agreements to participate in 7(a) lending with SBA. These participation agreements do not expire.

36. Is M&T training mandatory for CA SBLCs? Follow up: Does the SBA believe that such support would be critical for underserved borrowers?

Technical Assistance training is not mandatory for CA SBLCs but it is encouraged. SBA believes the support helps underserved borrowers start and grow their businesses.

37. What was the average number of loans, month by month, for Community Advantage lending from FY23 until YTD?

Community Advantage Approvals by Month (FY23 - 5/31/24)

Approval Month	# of Approvals	Approval Amount
202210	69	$ 11,070,700
202211	55	$ 9,964,000
202212	62	$ 10,640,800
202301	60	$ 11,820,600
202302	72	$ 12,321,300
202303	93	$ 17,156,000
202304	72	$ 12,611,000
202305	98	$ 17,121,600
202306	75	$ 12,973,700
202307	90	$ 15,140,800
202308	43	$ 8,044,300
202309	11	$ 2,444,200
202310	60	$ 10,832,000
202311	73	$ 14,198,200
202312	88	$ 15,494,700
202401	63	$ 11,807,800
202402	97	$ 19,179,100
202403	96	$ 16,365,000
202404	105	$ 17,893,800
202405	105	$ 18,668,900

Monthly Average	74	$ 13,287,425

38. What was the performance of similarly-sized loans in the Community Advantage Pilot Program and/or the CA SBLC Program as compared to those in the regular 7(a)?

See details below in Q39 response.

39. Please use all metrics that the SBA uses to measure performance for each full FY, starting in FY15 and ending in FY23.

	Early Default Rate (default amount within 18 months of disbursement divided by disbursement amount)		Cumulative Default Rate (default amount divided by disbursement amount)		Cumulative Purchase Rate (purchase amount divided by disbursement amount)		Cumulative Charge-off Rate (charge-off amount divided by disbursement amount)	
Disbursement Year	Community Advantage	7(a) Non Express loans up to $350k	Community Advantage	7(a) Non Express loans up to $350k	Community Advantage	7(a) Non Express loans up to $350k	Community Advantage	7(a) Non Express loans up to $350k
2015	3.8%	1.4%	16.4%	8.9%	13.4%	6.7%	8.9%	5.6%
2016	3.4%	2.2%	18.1%	10.0%	13.7%	8.1%	9.4%	6.6%
2017	2.3%	2.4%	14.4%	10.7%	11.7%	8.5%	7.5%	6.6%
2018	6.4%	3.1%	19.7%	11.1%	17.0%	8.8%	11.6%	6.6%
2019	3.9%	2.2%	15.4%	9.4%	12.8%	7.3%	7.2%	4.9%
2020	0.3%	0.9%	9.1%	5.7%	6.9%	3.7%	3.0%	2.0%
2021	1.0%	0.6%	6.4%	3.7%	2.7%	2.2%	1.7%	0.9%
2022	2.7%	2.3%	6.0%	4.0%	3.2%	1.8%	1.0%	0.5%
2023	2.1%	2.2%	2.1%	2.2%	0.9%	0.8%	0.3%	0.2%

40. How many of the CA SBLCs have done more than 10 loans since they converted to CA SBLCs?

15 CA SBLCs have approved more than 10 loans since being converted to CA SBLCs.

41. What written guidance has been provided to CA SBLCs regarding maximum loan size, and area of operations?

Maximum Loan Size: The maximum loan size was conveyed to the Lender's in Press Release 23-24 and is routinely reiterated during SBA presentations, such as the April 2024 Bi-Monthly Call for CA SBLCs and during a session at the May 2024 NADCO conference. In addition, E-Tran will not allow an application to proceed that exceeds the maximum loan size for CA SBLCs.

Area of Operations: The email/approval letter sent to each CA SBLC that accompanied SBA Form 750, Deferred Participation Agreement, advised the CA SBLC of its area of operation. In addition, E-Tran will not allow an application to proceed if the project is located outside the CA SBLC's approved area of operation.

42. You said in your testimony that if you could waive a magic wand and change anything at the SBA, you would want "better access to tax data." Because the SBA waives the need for lenders to verify tax transcripts on loans $500,000 and below, what is the tax data you would like, and how would the tax data be utilized at the Office of Capital Access?

Speaking specifically to the role of IRS tax data for our business loan programs: IRS tax data is also a strong internal control utilized to help mitigate fraud, a lesson learned from the CARES Act during the COVID-19 EIDL program when, under the previous Administration, Congress removed IRS tax data checks that contributed to high rates of fraud in pandemic programs. For 7(a) loans $500,000 or less, SBA allows lenders to either use IRS tax transcript data or business tax returns in their processes. Many 7(a) lenders prefer to use IRS tax transcript data because they feel it is more reliable than borrower-provided tax returns that can be digitally altered. Additionally, SBA requires IRS tax transcript data for all 7(a) loans greater than $500,000 as well as for all 504 loans of all sizes. Prudent loan underwriting requires the use of historical business financial performance, such as gross revenues, net profit, etc., to ascertain an appropriate loan amount that the business will be able to repay successfully. Additionally, businesses meet SBA's size standards using the number of employees, gross revenues, net worth, and net income, which are also provided in tax transcript data. Having access to this data makes SBA's determination of eligibility for size more reliable.

Risk:

43. Last year, the SBA implemented a new Risk Mitigation Framework after the SBA cited a need to streamline the eligibility process. How has the Risk Mitigation Framework been funded and what are the highlights of the results thus far? Follow up: Does SBA have goals for how quickly these 7(a) loans that are subject to eligibility checks should be processed?

The Risk Mitigation Framework is funded by multiple sources including salaries and expenses for staff, the Fiscal Transfer Agent (secondary market fees), and financial systems oversight funds. In summary, the Risk Mitigation Framework has provided an extra layer of fraud and compliance due diligence for lenders, SBA, and taxpayers. SBA works to ensure that loan applications are processed in a timely manner while ensuring that all fraud and compliance due diligence is conducted thoroughly.

44. Is SBA meeting its internal goals?

Yes.

45. How many safety and soundness checks have you done on the SBLCs in the last 2 years? Follow up: Do any of your safety and soundness checks rely upon self-certification?

For SBLCs, between May 29, 2022 and May 29, 2024, OCRM issued 4 Safety & Soundness Examinations and 30 Risk-Based Review Reports.

SBLC's are routinely asked to provide certifications, such as the quarterly "Certification of Compliance" where the SBLC must furnish SBA with a calculation of capital and certification of compliance with its minimum capital requirements.

46. How many full-time employees are currently at OCRM? Follow up: Is OCRM fully staffed?

As of July 25, 2024, OCRM had 39 full time employees. SBA is working to fill additional vacancies as we have shared with the Committee.

47. Early default rates have more than doubled in the last year. Can you please confirm what are the current early default rates? Follow up: Why do you think that is happening? Are those early defaults concentrated in the smallest loans?

SBA calculates an early default rate based on the dollar amount of loans disbursed in the previous 36 months that defaulted in their first 18 months on book. This rate has increased from 0.42% to 0.92% in the last year. The historic average is 1%. There are many contributing factors, including the current interest rate environment and the changing financial position of small businesses after many received an influx of capital during the pandemic. The increase can be interpreted as a regression toward the mean, or a return toward "normal" pre-pandemic rates. While small dollar loans do have slightly higher early default rates, most early default dollars come from larger loans.

Post-forgiveness reviews:

48. We understand that the SBA is now conducting thousands of post-forgiveness reviews on PPP loans. SBA has 90 days to review a PPP forgiveness application. Do you acknowledge that the SBA previously made final forgiveness decisions on the same loans they are now re-reviewing? Follow up: Is the SBA auditing its own decision-making by performing post-forgiveness reviews?

SBA is conducting post forgiveness reviews of certain transactions that are either part of an OIG recommendation to review forgiven loans or are being reviewed for some other reason, such as a loan that was flagged post-forgiveness.

49. Do you agree that there should be a distinction between fraud and borrower error? Follow up: What portion of your post-forgiveness reviews have you found that are a result of fraud?

SBA agrees there is a distinction between fraud and borrower error. Where it is clear that there is a borrower error, SBA considers partial forgiveness. While SBA relies on law enforcement to determine if it is actually fraud, SBA does not grant forgiveness if there is an indication of likely fraud.

Based on reviews performed so far, about 75% of the post-forgiveness reviewed cases are likely fraud.

50. What portion of your post-forgiveness reviews have you found that are a result of error?

Based on reviews performed so far, 17% of the post-forgiveness reviewed cases are borrower error.

51. Has there ever been any official SBA loan documentation or communication that explained that the SBA may reverse forgiveness decisions?

86 FR 8283 states that SBA may undertake a loan review at any time, including after forgiveness.

52. How long is a post-forgiveness review expected to take for the SBA to decide on whether or not it agrees with its original decision on the amount of forgiveness that a borrower received?

SBA is currently working to reduce the inventory of post-forgiveness reviews and strives to attain a 90-day turn-time as the inventory is reduced.

53. Are you going to tell PPP borrowers that their loans are going to be subject to post-forgiveness reviews? Why or why not?

SBA regularly communicates with the lenders who made and/or hold the PPP loans and expects the lenders to communicate with the borrowers based on the structure of the PPP program.

54. If forgiveness is reversed, what will this process look like for lenders? Follow up: What will this process look like for the borrowers?

SBA will be issuing guidance in the coming months.

55. At any time, did the SBA instruct lenders to mark the PPP borrowers' notes as paid and full after receiving forgiveness for the amount that was originally determined? Follow up: How can a lender collect on a note that has already been marked paid and full?

Procedural Notice 5000-20077 instructed lenders to mark the borrower's note for the PPP loan as "Paid in Full" and include the note in the notification to the borrower when SBA remits a forgiveness payment for the full amount of the PPP loan.

SBA will be issuing guidance in the coming months.

56. The Truth in Lending Act and other regulations require certain notice, disclosure, and timing requirements for banks issuing loans. How would banks be able to collect on these loans without violating these regulations?

SBA will be issuing guidance in the coming months.

COVID EIDL and PPP:

57. As the head of the Capital Access for the Small Businesses Administration, would you say the risks presented by the COVID EIDL and PPP were Identical?

Despite their differences, the PPP and COVID-19 EIDL programs have similar characteristics. The programs both provided loans needed to assist businesses during the COVID-19 pandemic. PPP loans of all sizes have no collateral and no guaranty. COVID-19 EIDLs have no collateral on loan sizes of $25,000 and below, and only limited UCC collateral for loans sizes above $25,000 up to $200,000.

58. Can you please explain why the SBA only performed an analysis of PPP loans to validate its decision to end active collections on loans valued at $100,000 or less?

Despite their differences, the PPP and COVID-19 EIDL programs have similar characteristics. PPP loans of all sizes have no collateral and no personal guaranty. COVID-19 EIDLs have no collateral on loan sizes of $25,000 and below, and only limited UCC collateral for loans sizes above $25,000 up to $200,000. For analyses on these portfolios, SBA evaluated the PPP program for cost benefit analysis for referral to the Treasury as more historical data was available that better simulated the PPP portfolio.

59. The SBA's 2025 budget requests $344 million to service COVID EIDL loans. This is a huge amount of money that would transform the mission of the SBA and its employees. Given this substantial cost, why didn't the SBA more seriously consider alternative options like selling the portfolio? Follow up: Why did the SBA retain an independent third party to assess the viability of selling this portfolio, if it were not going to take its recommendations seriously?

SBA evaluated the performance of the COVID-19 EIDL portfolio to calculate subsidy needs, to make strategic program management decisions, and to maximize a positive outcome for American taxpayers. SBA has explored all options to meet the mission, including whether it is cost effective to sell the COVID-19 EIDL portfolio to the private sector or whether SBA should service these loans in-house.

Based upon a recent analysis finalized in April 2024, SBA has determined that it is most cost-effective for American taxpayers for the portfolio to be serviced in-house at SBA. SBA will continue to monitor the portfolio's performance.

60. Although the Committee is pleased that the SBA reversed its disastrous policy decision not to refer delinquent pandemic loans of $100,000 or less to the Treasury, we are very concerned that the SBA again failed to provide a suitable analysis to justify an important policy decision. Why was an independent analysis not performed for COVID EIDL?

Despite their differences, the PPP and COVID-19 EIDL programs have some similar characteristics. PPP loans of all sizes have no collateral and no personal guaranty. COVID-19 EIDLs have no collateral on loan sizes of $25,000 and below, and only limited UCC collateral for loans sizes above $25,000 up to $200,000. For analyses on these portfolios, SBA evaluated the PPP program for cost benefit analysis for referral to the Treasury as more historical data was available that better simulated the PPP portfolio. As the PPP portfolio demonstrated its collectability and showed that it would be cost-effective to refer the delinquent PPP debts to the Treasury, then the same calculations would translate to COVID-19 EIDL.

61. You said in your testimony that the agency is finalizing an analysis of a potential sale of COVID EIDL, and that it would be shared with the Committee once complete. Can we expect this analysis next month? If not, please provide a timeframe for when the Committee will be able to see this analysis.

SBA evaluated the performance of the COVID-19 EIDL portfolio to calculate its cost, to make strategic program management decisions, and to maximize a positive outcome for American taxpayers. SBA has explored all options to meet the mission, including whether it is cost effective to sell the COVID-19 EIDL portfolio to the private sector or whether SBA should service these loans in-house.

Based upon a recent analysis finalized in April 2024, SBA has determined that it is most cost-effective for American taxpayers for the portfolio to be serviced in-house at SBA. SBA will continue to monitor the portfolio's performance.

62. The OIG has often described the SBA's data tracking in various portions of the COVID lending programs to be "ad hoc." What has the SBA done to maintain more accurate and more useful data regarding these loans?

The new Unified Lending Platform allows for enhanced on-demand data tracking. A bi-weekly executive briefing contains data on delinquency rates, HAP enrollments, call volumes, and staffing numbers for COVID EIDL to actively monitor loan performance.

63. How has the SBA's initial decision to not collect on loans valued under $100,000 impacted its ability to detect and collect fraudulent funds?

SBA always collected on all COVID-19 EIDL loans. We assume this question refers to SBA's previous process, which did not include Treasury referrals for PPP and COVID-19 EIDL loans of $100,000 or less.

There has been no impact and no change for likely fraudulent loans, which cannot be referred to Treasury due to Treasury's regulations. SBA continues to treat all likely fraudulent loans the same regardless of loan amount. If suspected fraud is identified, the loan is flagged and referred to SBA OIG.

64. In the SBA's April 2022 memo that discussed the end of active collections on PPP and EIDL loans valued at $100,000 or less, it indicated that it was "ending all collection activities on the subject loans." The SBA later contradicted itself by claiming that it was still performing 13 of its 14 collection tasks. Can you please clarify what the SBA was and was not doing regarding delinquent COVID-19 and PPP loans at $100,000 or less, since April 2022?

There is no contradiction: SBA has always collected on all COVID-19 EIDL loans, but we paused a final step of referring to Treasury until we determined that it was a cost-effective collection measure. Please refer to our letters to Chairman Williams on March 27, 2023, November 1, 2023, and February 9, 2024.

65. In its April 2022 Memo, the SBA stated twice that it was going to "end collections," on loans $100,000 or less, "including referral to treasury." Additionally, in response to the SBA OIG Report in Sept. 2022, the SBA stated again that it had "ended collection" on these loans. The SBA used the phrase "ending collection" again in a March 2023 letter to the Committee. We have since been told that the SBA did not end collection on these Loans. Can you please explain if the SBA was collecting on these loans, and if so, how was the SBA treating delinquent loans valued at $100,000 or less?

See answer to #64. Associate Administrator Frost briefed the Committee staff in December 2023 and January 2024 on this issue.

66. A consultant hired by the SBA also said that retaining the portfolio would represent a "Dramatic shift of SBA's mission to a loan servicing operation." Does the SBA want to become a loan-servicing operation?

SBA already services loans throughout our Disaster Loan Program. SBA established the COVID-19 EIDL Servicing Center (CESC) in early FY23 specifically to service the COVID-19 EIDL portfolio. The CESC is very successfully servicing the portfolio with the highest standards of customer service and accountability and in accordance federal credit standards. There is no detraction from the SBA mission by the CESC or any of its resources or responsibilities.

67. In an email exchange between the SBA and the Department of Treasury, the Treasury asked what the servicing needs of the $100,000 and under loan portfolio would be. The SBA indicated that 90-day delinquent loans would be charged off, with other loans receiving "general collection activity." Can you please explain what "general collection activity" means here?

General collection activity includes weekly collection emails, weekly collection phone calls, and paper mail due process notices. The collection emails and calls include information on enrolling in the hardship

accommodation plan that allows distressed borrowers to lower their monthly payment for up to 24 months.

68. The SBA notified the committee that they reached an agreement with Treasury a few weeks ago which would add tasks that normally fall under Treasury's responsibilities, to the SBA. Why did the SBA agree to take on more responsibility for these loans? Follow up: You keep telling Congress you need more money to service these loans, and now you are taking on more responsibility, how much more will it cost? Where will that money come from?

SBA and Treasury agreed that it would be most beneficial to COVID-19 EIDL defaulted borrowers to remain with SBA to attempt workout and restructure of their debts given that SBA has tools that are not available through Cross-Servicing that it can leverage for the COVID-19 EIDL debts, and SBA has broad powers to service COVID-19 EIDLs and the resulting debts, including taking any and all action determined necessary or desirable in "making, servicing, compromising, modifying, liquidating, or otherwise dealing with or realizing on [such] loans." 15 U.S.C. § 634(b)(7). SBA will continue to transfer to Treasury Cross-servicing those debts that are nonresponsive to SBA's collection efforts.

SBA will continue transferring all defaulted COVID-19 EIDL debts to Treasury for offset under the Treasury Offset Program (TOP) as it has traditionally done with its traditional Disaster Loan Program loan portfolio.

69. Does this change the cost/benefit analysis about selling the COVID EIDL portfolio?

No.

70. Please describe the assumption regarding collectability and default rates that the SBA made in its initial analysis of the PPP program, which indicated that the SBA should not take collection activity.

Please see the answer to #71 for a discussion of the different assumptions between the two analyses.

71. Please describe the assumption regarding collectability and default rates that the SBA made in its follow-up analysis of the PPP program, which indicated that collections would be more affordable to the taxpayer.

Several key differences in the updated analysis as compared to the earlier analysis:

1. Population size (at the time of analysis): $7.2B and 439K loans, including $5.1B potentially recoverable.
- Earlier analyses: $1.4B, 80K loans

2. Methodology: Divide PPP guaranty purchased population into potentially recoverable and unrecoverable populations, and within recoverable, apply unique recovery rates based on borrower entity type.
- Earlier analyses: Apply historical average recovery rate estimate for proxy population of loans to full PPP purchase population. Assume 10% of the PPP purchase population will be forgiven and therefore be ineligible for recovery.

3. Proxy population and data analyzed: SBA Express <$100K to sole props, 2009-2012; as well as 7a and ARC loans <$100K, 2009-2012; and PPP >$100K

- Earlier analyses: SBA Express <$100K to sole props, 2009-2012; Public filings (i.e., Forms 10-K) from large debt buying companies

4. Length of time remaining on maturity period: ~3.5 years
- Earlier analyses: ~5 years

72. Please describe what the SBA learned regarding its financial modeling and analytical approach that made its initial analysis incorrect, and how the lessons learned will be used to improve future programs.

SBA used the best data and information available at the time of each analysis to analyze collectability. The Agency also strengthened the analyses each time we explored this question by building on past results. Other contributing factors, such as the improved economy, and the ending of rolling deferment periods have provided repayment data. SBA is on a continuous self-improvement path as it utilizes experience and improved technology to deliver a more streamlined and cost-effective lending experience to borrowers.

Miscellaneous:

73. How many SBA loans exist for small businesses that are federally licensed firearm retailers/dealers?

As Associate Administrator Frost testified at her hearing, SBA tracks lending by NAICS codes. Federal firearms licensees do not have a unique NAICS code making the data difficult to track, and they may include pawn shops, sporting goods stores, miscellaneous retail, and other NAICS codes that would also include many businesses that do not sell firearms.

74. There have been multiple recent reports from small businesses in the firearm industry that have been denied access to SBA loans and the stated reason given was they were a firearm industry business. You testified during the May 15th hearing that "loan programs at SBA support all types of small businesses across different industries, including those who would sell firearms." Based off these recent reports, have you been made aware of cases since the May 15th hearing that contradicts your testimony? In light of these recent reports, for the record, does the SBA have a policy (written or unwritten) that discriminates against the constitutionally-protected firearm industry?

SBA is not aware of any cases of SBA loan declines because the business sells firearms. SBA business loans are administered through private sector lenders. SBA does not have any policy or requirement limiting or restricting loans specifically for businesses involved in firearm sales.

75. Does SBA partner with lenders that have policies that discriminate against the firearm industry?

Lenders set their own policies on which businesses they will lend to, so long as they abide by SBA loan program requirements.

76. If it is learned that an SBA lender has a policy that discriminates against an industry lawful under federal law, including the constitutionally-protected firearm industry, how does this impact their eligibility standing as an SBA lender?

SBA places requirements on certain industries to ensure they meet all applicable laws and regulations for their industry. For example, several industries (liquor sales, care providers, exporters, etc.) require licenses and SBA requires lenders to check for such licenses. Another example is the specific requirements for gas stations. Please see Appendix 7 to SOP 50 10 7 for more information on requirements pertaining to gas stations.

All SBA loans are subject to all applicable laws, including (without limitation) the civil rights laws, prohibiting discrimination on the grounds of race, color, national origin, religion, sex, marital status, disability or age. Not lending to borrowers in an industry would not likely be a violation of those requirements and would not affect the SBA Lender's standing. In fact, lenders sometimes decide to avoid lending to certain industries due to risk factors and other concerns.

77. What do you say to members of the firearm industry who have been denied access to SBA loans because they are members of the firearm industry, and do they have any recourse to reverse the decision?

SBA provides government-backed loans, but the decision on whether to lend to a business is determined by the lender based upon their analysis of the business eligibility for the SBA's loan programs. Small businesses seeking SBA loans can work with any SBA lender, and Lender Match is a great tool to match with potential sources of capital.

78. To be eligible for a SBA loan, a business, among other criteria, "must be creditworthy and demonstrate a reasonable ability to repay the loan." What is the minimum credit score needed?

There is no minimum credit score for SBA business loans. For loans under $500,000, SBA uses the FICO® Small Business Scoring Service Score (SBSS Score) model and requires a score of 155 or better to move forward with streamlined processing. SBA provides an alternative method of underwriting loans that do not achieve the minimum credit score. For all other 7(a) loans, and for 504 loans of all sizes, SBA requires more extensive underwriting that examines a number of factors in totality.

79. Has the SBA met with, spoken to, or in any other way coordinated or communicated with the White House office of gun violence prevention, or the bureau of alcohol, tobacco, and firearms on SBA programs?

SBA regularly meets with the interagency on issues pertaining to its loans, products, and services.

80. If so, what changes to SBA programs were discussed or proposed? Provide copies of any communications by between and among SBA, ATF and WH OGVP discussing or referencing SBA loans to FFLs.

See above answer to Q 79.

812. Has the SBA met with any other federal agency that regulates small businesses in the firearm industry?

See above answer to Q 79.

82. Has the SBA discussed restrictions on lending to small businesses in the firearm industry?

As Administrator Frost testified, SBA's loan programs support all types of small businesses across industries, including those involved in the firearms industry. SBA does not have any policy or requirement limiting or restricting loans specifically for businesses involved in firearm sales.

Questions from Rep. Blaine Luetkemeyer (R-MO-03)

1. When the guardrails were put on the 7(a) program over the last three decades, the subsidy rate declined. Yet, when SBA removed many of the guardrails, there was no impact to the subsidy rate. How can that be?

SBA simplified an unnecessarily complex set of rules and procedures for the 7(a) Loan Program that will assist in attracting and retaining more lenders for the program and lower the cost of making small dollar loans. Lenders will continue to be required to make, close, and service loans in a prudent manner and may only make 7(a) guaranteed loans where repayment ability is reasonably assured from the operations of the business.

2. Ms. Frost, what was your role in the Funding Circle selection to be an SBLC? Did Patrick Kelley set up the selection process before he left the Agency? Is Mr. Kelley still involved with Funding Circle in any capacity. If he is, the appearance of a conflict would be unquestionable and could lead to a Congressional investigation and a referral to the Inspector General.

Patrick Kelley left government service over a year ago and prior to Funding Circle's selection as one of the new SBLCs. The SBLC selection process was outlined in detail in a May 14, 2024, letter to the Committee, and Associate Administrator Frost testified that the SBLC selection process and license vote was led by a team of career SBA officials.

Effective June 24, 2024, Funding Circle voluntarily surrendered its SBLC license. Funding Circle announced the sale of their US operations to iBusiness Funding LLC, a division of Ready Capital Corporation. ReadyCap Lending LLC already holds an SBLC license.

Questions from Rep. Tracey Mann (R-KS-01)

There have been multiple recent reports from small businesses in the firearm industry that have been denied access to SBA loans and the stated reason given was they were a firearm industry business. You testified during the May 15th hearing that "loan programs at SBA support all types of small businesses across all different industries, to include those who would sell firearms."

1. Based off these recent reports, have you been made aware of cases since the May 15th hearing that contradicts your testimony? In light of these recent reports, for the record, does the SBA have a policy (written or unwritten) that discriminates against the constitutionally-protected firearm industry?

As Administrator Frost testified, SBA's loan programs support all types of small businesses across industries, including those involved in the firearms industry. SBA does not have any policy or requirement limiting or restricting loans specifically for businesses involved in firearm sales.

2. Does SBA partner with lenders that have policies that discriminate against the firearm industry?

As Administrator Frost testified, SBA's loan programs support all types of small businesses across industries, including those involved in the firearms industry. SBA does not have any policy or requirement limiting or restricting loans specifically for businesses involved in firearm sales. Lenders set their own policies on which businesses they will lend to, so long as they abide by SBA loan program requirements.

3. If it is learned that an SBA lender has a policy that discriminates against an industry lawful under federal law, including the constitutionally-protected firearm industry, how does this impact their eligibility standing as an SBA lender?

See answer to Question 76 above.

4. What do you say to members of the firearm industry who have been denied access to SBA loans because they are members of the firearm industry, and do they have any recourse to reverse the decision?

See answer to Question 78 above.

5. To be eligible for a SBA loan, a business, among other criteria, "must be creditworthy and demonstrate a reasonable ability to repay the loan." What is the minimum credit score needed?

See answer to Question 79 above.

6. Has the SBA met with, spoken to, or in any other way coordinated or communicated with the White House office of gun violence prevention, or the bureau of alcohol, tobacco, and firearms on SBA programs?

See answer to Question 79 above.

7. If so, what changes to SBA programs were discussed or proposed? Provide copies of any communications by between and among SBA, ATF and WH OGVP discussing or referencing SBA loans to FFLs.

See answer to Question 79 above.

8. Has the SBA met with any other federal agency that regulates small businesses in the firearm industry?

See answer to Question 79 above.

9. Has the SBA discussed restrictions on lending to small businesses in the firearm industry?

See answer to Question 82 above.

10. In addition to providing me with the number of federally licensed firearm retailers with SBA loans, of those, how many are designated as veteran-owned?

See answer to Question 73 above.

11. What additional eligibility requirements do federally licensed firearm retailers have to be designated as veteran-owned by the SBA? Are any of these requirements different based on industry?

To determine an applicant's status as a veteran, SBA follows the definitions in Title 38, Section 101(2), (10) , and (18), and which is posted in SOP 50 10 7.1, page 364, which states A person who served in the active military, naval, or air service (i.e., the United States Army, Navy, Marine Corps, Air Force, and Coast Guard, including the reserve components thereof), and who was discharged or released therefrom under conditions other than dishonorable. The term "discharge or release" includes (A) retirement from the active military, naval, or air service, and (B) the satisfactory completion of the period of active military, naval, or air service for which a person was obligated at the time of entry into such service, or, in the case of a person who, due to enlistment or reenlistment, was not awarded a discharge or release from such period of service at the time of such completion thereof and who, at such time, would otherwise have been eligible for the award of a discharge or release under conditions other than dishonorable. These requirements apply across different types of businesses and SBA programs.

Businesses in many different NAICS sectors may be licensed to sell firearms. For example, in many states, Walmart sells firearms. Pawn shops sell firearms as well. SBA requires that any business have all the licenses required to operate. This is a matter of prudent underwriting because the lender is relying on the business's ability to successfully operate so that it can repay the loan.

12. Would applying for veteran designation as a federally licensed firearm retailer automatically trigger a denial? If no, what would make a federally licensed firearm retailer ineligible for veteran designation?

As stated above, the two are not related.

13. What is the process for a small business to obtain a veteran-owned status from the SBA?

In the 7(a) loan program, businesses owned by veterans are exempt from paying the upfront SBA guaranty fee in the 7(a) SBA Express Program. These lenders verify the applicant's DD 214 to confirm veteran status. In the 504 program, the 504 Certified Development Company that makes a loan to a business owned by a veteran will be meeting one of the public policy goals as outlined in 13 CFR 120.862(b)(4).

14. Are there any industries ineligible for veteran-owned status?

No.

Questions from Rep. Nydia Velázquez (D-NY-07), Ranking Member

Associate Administrator Frost, according to your testimony the SBA has approved more than 22,000 7(a) loans under $150,000 in FY' 24, which is a 30 percent increase over last year. I applaud Administrator Guzman and the SBA's effort to increase small dollar lending. As you know, this has been something I have encouraged the SBA and our lending partners to do for a long time.

1. Can you speak to how the SBA intends to increase these number even further in FY' 25?

The 7(a) Program changes from FY23 will continue to produce a higher volume of small loans as lenders fully implemented the changes during late FY23 and FY24. Additionally, SBA envisions the new SBLCs will focus primarily on small dollar lending.

2. How is the SBA tracking these originations to ensure small businesses in underserved communities—particularly urban communities of color, rural communities, and native communities—receive access to these loans?

Community Advantage Small Business Lending Companies (CA-SBLCs) have responded with enthusiasm to the CA-SBLC license, and Community Advantage lending has taken off as a result. Through the second quarter of FY24, CA lending is up 17% compared to the same period in FY23.

SBA has spent the last several years identifying and reducing barriers to obtaining loans faced by communities whose access to these loans have been historically and disproportionately low. SBA has addressed burdensome program requirements (e.g., streamlining forms) with the main focus of increasing the utilization of loans by borrowers, including underserved borrowers. All 7(a) and 504 lenders, not just CA SBLCs, can and do make loans to underserved borrowers. In fact, due to their nationwide reach and large on-the-ground footprint, the biggest lenders make the most loans to underserved borrowers. SBA has tangible results to show for these efforts. As of March 31, 2024, the year over year (fiscal year) comparison indicates: For the entire 7(a) portfolio, an increase in the number of loans (of all sizes) from 26,381 to 31,293; for 7(a) loans $150,000 or less, an increase from 13,089 to 17,550 loans; for 7(a) loans $150,001 to $500,000, an increase from 7,121 to 7,723 loans.

3. How is the Office of Capital Access working with SBA's regional offices to raise awareness amongst small business owners and entrepreneurs of the availability of smaller dollar loans?

OCA communicates updates with and through SBA's Office of Field Operations (OFO) regularly—including supporting weekly OFO management meetings and monthly stakeholder meetings focused specifically on OCA updates. OCA also hosts internal training on our loan programs and works with individual field offices regularly.

4. For FY' 25, the SBA is requesting approximately, $397,00 in S&E funding, which includes personnel. This represents almost a $71,000 increase over FY '24 levels. How does this increased funding enable OCA and OCRM to oversee the activities of the three new SBLCs that were just issued? Does SBA have enough staff to properly oversee seventeen SBLCs?

The 2025 Budget requests the necessary resources to operate all SBA programs, including lender oversight for our loan programs. With the recent staffing additions and ongoing recruiting efforts, OCRM is adequately staffed to oversee the SBLCs.

5. Last month Administrator Guzman told this Committee that the SBA would revoke the SBLC license from Funding Circle if Funding Circle US is sold to a third party that the SBA does not approve of. Is that still the current position of the SBA?

On June 24, 2024, Funding Circle sold their US operations to iBusiness Funding LLC, a division of Ready Capital Corporation. ReadyCap Lending LLC has an existing SBLC license with an existing relationship with SBA. Before the sale agreement was executed, FC SBA Lending LLC voluntarily surrendered its SBLC license to SBA because ReadyCap Lending LLC already holds an SBLC license.

6. Do you think granting Funding Circle an SBLC license now sets a troubling precedent whereby in a corporate transaction the monetary value is associated with the SBLC license not the loan portfolio?

SBLC licenses have been bought and sold on the private market for decades. SBA does not determine what price a buyer is willing to pay a seller, but as a regulator we ensure that any license transfer is to a lender that meets SBA standards and we have blocked the transfer of licenses in the past when entities did not meet SBA requirements.

Effective June 24, 2024, Funding Circle voluntarily surrendered its SBLC license.

7. Associate Administrator Frost, three lenders—Arkansas Capital Corp., Alaska Growth Capital, and Funding Circle—were recently awarded SBLC licenses. However, can you tell us how many lenders applied to the SBA for an SBLC license? Can you explain the metrics and the process SBA used to evaluate the applicants and ultimately award the licenses to these lenders?

The applications were evaluated on qualitative and quantitative measures based on capitalization, management team, business plan, and historical performance (if any) as well as market gap measures based on the SBA's focus on underserved communities and small loans.

The applications went through a multi-step evaluation process:

Step 1: All applications were accepted and reviewed initially by a Due Diligence Committee, starting with a Loan Specialist from the LGPC who worked with the applicant(s) to ensure they responded to all the items listed in the Federal Register Notice. The Loan specialist then prepared a recommendation memo and scoring matrix for review by the Due Diligence Committee (DDC) and included a qualitative score and a market gap score. The DDC then put each SBLC applicant into one of three buckets: Incomplete, Recommended for Consideration, or NOT Recommended for Consideration. The DDC was comprised of 6 career employees: 3 from OFPO (one of which was the Loan Specialist assigned to do the initial file review), 2 from OFA, and 1 from OCRM. The DDC was overseen by the 7a Loan Guaranty Processing Center (LGPC) Deputy Center Director. All the applications were reviewed and scored individually and then reviewed one last time as a group for comparison purposes.

Step 2: The results were then presented to the Review Committee (see attached recommendation PP) which was comprised of the License Committee as well as other leaders from within SBA including OCA, OGC, CFO, OII, OCFO, OVBD, OWBO, and the front office. The Review

Committee reviewed memos from the DDC, asked questions, and provided additional perspective on potential SBLCs.

Step 3: The License Committee, composed of the career Deputy Associate Administrator for OCA, the Director of the Office of Financial Assistance, the Director of the Office of Financial Program Operations, the Director of the Office of Credit Risk Management, and the Director of the Office of Performance and Systems Management, voted to select the new SBLCs. All five are career members of the Senior Executive Service within OCA. See the attached Review Committee Memo to file memorializing the Licensing Committee's final actions.

Onboarding: Once the Licensing Committee tentatively awarded the license, each applicant went through OCRM for final vetting including review of the applicant's credit policies and internal control policies as well as verification of the minimum capitalization.

8. Associate Administrator Frost, Funding Circle's head of Public Affairs, Mr. Ryan Metcalf, has stated that he "expects [Funding Circle] to be able to start lending in April." Can you explain how the SBA is working to ensure that Funding Circle carries out the purpose of the SBLC license, which is to provide 7(a) loans?

Funding Circle did not make any 7(a) loans before they voluntarily surrendered their SBLC license on June 24, 2024.

9. Associate Administrator Frost, as has been reported, Funding Circle reported losses of approximately 3.9 million Pounds in 2023. Do you think granting a lender with significant losses and questions about its capital adequacy sets a concerning precedent for future lenders? Are we setting a precedent whereby lenders with inadequate capital levels and significant losses can be let into the program?

Lenders must meet SBA capitalization requirements to participate in SBA lending. All of the selected organizations to become SBLCs, including Funding Circle, met those requirements.

For SBLC transfers of control or ownership, it is common for a change of control applicant to present a business plan that projects operating losses for the first several (2-4) years until the licensee's SBA loan portfolio reaches a size and annual origination volume that is self-sustaining.

10. Associate Administrator Frost, your testimony states that in FY '24, to date, the SBA has "approved more than 22,000 7(a) loans under $150,000," which is "a 30% increase compared to this time last year." While it is still early, what percentage of these loans have defaulted? How do these defaults compare to the percentage of defaults in the overall 7(a) program?

As of August 1, 2024, 6 loans approved in FY24 with loan amounts up to $150,000 have defaulted (0.05% of disbursed loans in this category). In comparison, 4 loans approved in the same time period for greater than $150k have defaulted (0.04% of disbursed loans in this category). This low level of defaults is consistent with program performance this early in the loan cycle.

11. Associate Administrator Frost, your testimony states "SBA has enrolled three new private sector lenders through the SBLC program to increase the supply of capital, each of which demonstrated through the license application process a commitment to filling a particular market gap." With

regards to Funding Circle specifically, what market gap did they commit to filling and what evidence did they present in their application that showed their commitment to filling this gap?

The business plan submitted by Funding Circle stated they would focus on small dollar lending, especially loans under $500,000 and under $150,000. They would also seek to work with underserved communities by direct marketing, partnership with existing 7a lenders, and other means including identifying low-to-moderate income neighborhoods based on HUD data, and small businesses in rural areas based on Federal Housing Finance Agency data tables.

12. Associate Administrator Frost, in November 2023, Community Advantage mission-based lenders transitioned into Community Advantage SBLCs. SBA added 30 new CA SBLC lenders in 2023 for a total of 142 mission lenders. In partnership with these missioned-focused CA SBLCs, what are the SBA plans to increase lending to underserved markets, and in particular businesses that aren't able to access conventional 7(a) loans?

SBA's top CA-SBLC priority for the past six months has been ensuring our new CA-SBLC lenders have a strong foundation to succeed in the program and begin making 7a loans. To that end, the Agency recently finished a 16-hour training for all of the new CA-SBLCs.

13. Associate Administrator Frost, under the SBLC Moratorium Recission and Removal of the Requirement for a Loan Authorization rule, 141 Community Advantage SBLCs have been approved by the SBA. These lenders are required to make at least sixty percent of their loans to businesses in an underserved market. How is the SBA tracking 7(a) lending activity and specifically the targeted lending being done by Community Advantage SBLCs versus lending by SBLCs, versus 7(a) lending generally?

SBA Form 3518, "Community Advantage Addendum – 7(a) CA SBLC" is used in conjunction with SBA Form 1919 by CA SBLC Lenders. CA SBLC Lenders will collect information from the Applicant to track loans made to small businesses in underserved markets. CA SBLCs will be required to submit SBA Form 3518 as an addendum to SBA Form 1919 when submitting the 7(a) loan Application to SBA in E-Tran.

CA SBLCs must submit an annual report which will validate that the CA SBLC underserved markets requirements have been met.

CA SBLCs must also submit a Quarterly Condition Report which includes a reconciliation of the entity's SBA loan underserved market distribution.

14. Associate Administrator Frost, in both the FY' 24 Congressional Budget Justification and the FY' 22 Annual Performance Report, it states the SBA authorized additional grant funds to provide comprehensive training for new 7(a) Community Advantage Lenders and Microloan Intermediaries. Will the SBA offer additional training to newly designated CA SBLCs in FY' 25?

The previously authorized grant funds were extended and used to train all CA SBLCs including the newly designated CA SBLCs during FY 2024. Lenders received 16 hours of training focused on the regulations, policies and procedures for originating, servicing and liquidating SBA 7(a) loans. SBA has not discussed entering into any additional third-party contracts, however internal training opportunities will continue through webinars and the Training on Demand webpage.

15. Associate Administrator Frost, the SBA recently launched the enhanced Lender Match Platform. According to the SBA press release, the platform features nearly 1,000 SBA lenders, including 257 community-based lenders, who can connect to potential customers and earn their business. Of the 257- community-based lenders, 142 are mission-focused CA SBLCs, some of which have small staff capacity, making it more challenging to use this new tool. How will the SBA work with mission-driven and community-based lenders to improve how this tool can work for their organizations and support new SBA lending?

SBA has provided and will continue to provide one-on-one training to lenders at their request. This training will guide them through the tool and show them how to tailor to their specific needs. As a match making (not a loan application) tool, Lender Match provides leads to lenders that meet their criteria. The lender can decide if the applicant qualifies for a commercial loan or if they could qualify for an SBA loan guaranty.

16. Associate Administrator Frost, the SBA sunset the Community Advantage Loan Program in October 2023 to focus non-profit lenders on the Community Advantage CA SBLC program, which was created via SBLC Moratorium Recission and Removal of the Requirement for a Loan Authorization rule last year. The transition from the CA program to CA SBLC has not been without its challenges. Can you provide insight into how the SBA has worked with industry partners to address transitional challenges and ensure continuity of service to small businesses?

SBA has provided mandatory training to all newly designated CA SBLCs, conducts bi-monthly training calls specifically to CA SBLCs, quarterly training calls for all 7(a) lenders, and hosts a "Training on Demand" web page with recorded live training and downloadable slide decks on a variety of topics ranging from fundamental underwriting, program requirements, entering loans into SBA's electronic system, etc. As permanent 7(a) lenders, CA SBLCs are now making loans confident that the program in which they are investing time, personnel, and resources will not be sunset. And, because CA SBLCs are now using the regular Standard Operating Procedure from which all 7(a) lenders work, they have more training opportunities across a variety of trainers, from SBA to national trade groups and other professional trainers on SBA.

17. Associate Administrator Frost, it's my understanding the SBA's E-Tran system has not been fully updated to reflect all the changes in the most recent SOP and the Affiliation Rule from last year. Lenders have reported several problem areas that are slowing down the processing times for borrowers and creating confusion. Have you heard this concern? When can we expect the E-Tran system to be updated?

SBA's E-Tran system, the risk management platform, and SBA's forms gather data to comport with the changes in the SOP and the Affiliation Rule.

SBA's E-Tran system & the Risk Mitigation platform are adjusted to meet change issues raised by: SOP changes, Audit findings, & Management guidance. Given the multiple change requests OCA's It support group formally tracks and prioritizes updates in consultation with its Customers & Partners with the goal to minimize the impact of updates while reducing the risk of fraud. Since October 2023 OCA has implemented 70 Risk Mitigation updates and 40 SOP updates. Additionally, we have a lender relations team that assists with any questions or system adjustments.

Questions from Rep. Jared Golden (D-ME-02)

1. Administrator Frost, as it pertains to Economic Injury Disaster Loans (EIDL) and the Paycheck Protection Program (PPP), the use of the same application for both products has flagged many applications for fraud, causing delays in processing. Is SBA aware of this issue? If so, what actions are being taken to improve the application process? If not, does the SBA plan to develop a plan to address these issues?

There may be some confusion because the Economic Injury Disaster Loans (EIDL) and the Paycheck Protection Program (PPP) do not use the same application. For PPP, small businesses applied directly with PPP lenders. Whereas with EIDL, one of SBA's disaster loan products, disaster survivors apply directly through MySBA on an updated application that launched December 2023. Notably, the COVID-19 EIDL application was also a different system, which has since been decommissioned.

2. Administrator Frost, I'm concerned that my constituents are finding difficulty acquiring accurate information on the status of their loans when contacting the call center. Particularly given the issues my constituents are having with the new portal system. Are you aware of this issue? What steps, if any, is the SBA taking to ensure that callers inquiring about the status of their loans are receiving accurate information?

SBA is receiving positive feedback on the disaster loan call center and the center's performance metrics are strong. Please provide the names and application numbers for any constituents with concerns and OCA will check the status of their applications.

3. Administrator Frost, my staff works very closely with SBA district offices on outreach, information sharing, and other issues to ensure each small business gets their chance. However, I'm learning that State Directors have little access to loans in the new portal, making it difficult for constituents to get accurate information. Are you aware of this? Have State Directors voiced their concerns on this issue?

In transitioning from the legacy disaster loan application to the new application, internal reporting is shifting and some reports have changed. OCA is working closely with all disaster loan application data users, including field offices and State Directors, to ensure strong, consistent reporting is available for all who need it. OCA recently updated the public dashboard on disaster loan reporting, which now provides significantly more information than the previous public dashboard.

4. Administrator Frost, I've heard from my constituents that the SBA portal interface is not business or nonprofit-friendly, causing issues for constituents requesting tax transcripts and other necessary signatures. The new portal that was rolled out in January included new automation steps to make the process easier, however, because there is no accurate prediction of how long the automated process takes, it's caused uncertainty for constituents in my district. Not only that, these automated processes cannot be overridden, adding another barrier for loans that may require manually correcting. Has the SBA been aware of the issues with the new portal? Is the Agency taking steps to improve and fix the issues being brought up?

The new disaster loan application is providing a step-change improvement for disaster survivors seeking SBA loans. The new application is significantly more user-friendly in that it is designed mobile-first and includes key features like dynamic questioning so users only see the questions that are relevant for them. This change and others have contributed to users taking an average of only 16 minutes to complete the application. We also can decision applications and disburse funding significantly faster. On the legacy

system, it took upwards of 100 days for a disaster survivor to receive a disbursement after they applied, and now we've cut that down to around 30 days. We have plans to improve that even further.
Even with these incredible benefits, SBA is aware of some technical issues that arose during the transition to the new system and is diligently working through them.

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