U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

OFFICE OF THE ADMINISTRATOR

October 14, 2008

The Honorable Bruce Braley
U.S. House of Representatives
Washington, DC 20515

Dear Congressman Braley:

Thank you for your recent letter concerning the U.S. Small Business Administration's (SBA) October 2007 changes to the credit elsewhere test. I appreciate your offer to work together to ensure that the test is reasonable and I understand your concern for small businesses in Iowa and elsewhere in the Midwest. I have personally visited Iowa and met with small businesses and local officials, and I understand the obstacles they are experiencing in their efforts to recover.

As approved by Congress, the Small Business Act, Section 7(b), requires that borrowers who can obtain credit elsewhere receive disaster loan assistance at the higher rate and, in the case of businesses, a shorter term for repayment of their loan. The credit elsewhere test is the result of this statutory requirement. Our goal in administering the disaster loan program is to have a fair measure of whether or not a disaster loan applicant can obtain credit elsewhere.

In particular, I share your concern about small businesses that the agency may have deemed as having credit available elsewhere, but that have not been able to obtain credit at reasonable market rates in the private marketplace. For this reason, I have provided guidance to the field to clarify the applicability of the hardship waiver test. This notice will remind SBA loan officers to ensure business borrowers are reviewed to determine if the higher credit available elsewhere rate and limited term imposes undue financial hardship. For the 67 small businesses in Iowa who qualified for the higher credit available elsewhere rate, the Agency will immediately review the loan applications for these businesses to ensure the credit elsewhere test was properly applied and, where appropriate, whether or not a financial hardship waiver should be considered. In cases where SBA will be able to grant a financial hardship waiver, a new loan with a lower interest rate and longer terms will be offered to the small business.

I also appreciate the opportunity to clarify the data that has been misrepresented in several press accounts regarding SBA's disaster loans in Iowa. As of October 7, 2008, the Agency has approved 3,522 disaster loans totaling $237,651,500 in Iowa. Fully 71 percent of these SBA disaster loans, representing 87 percent of total loan dollars, are at the lower, credit not available elsewhere rate.

Specifically regarding businesses accessing SBA's disaster loan program in Iowa, 89 percent are at the lower, credit not available elsewhere rate. Eleven percent of business loan applicants (67 businesses), representing just 6 percent of business loan dollars, qualified for the higher, credit elsewhere rate. For these 67 businesses in a stronger financial position, a three-year loan term is mandated by law and not subject to change without legislation from Congress. As pointed out in a letter from the Senate, several of these businesses have found better loan terms in the marketplace. This is evidence that supports the Agency's determination that those specific applicants do have the ability to secure credit elsewhere and by law, are eligible only for the higher credit elsewhere available rate.

As required by the law, SBA implements the credit elsewhere requirements to ensure the Federal Government is not displacing or competing with valid private sector options. SBA has not changed its position with regard to the need to examine the overall financial conditions of the borrower as a part of the credit elsewhere test. The percentage of applicants who qualify for the lower credit not available elsewhere interest rate will vary based on their financial solvency and their ability to meet the asset requirements. For homeowners in Iowa seeking assistance from SBA, 67 percent qualify for the lower credit not available elsewhere rate, leaving 33 percent of the homeowners who are eligible for the credit available elsewhere rate, which, at 5.375 percent is still below the market rate. Additionally, the loan terms provided by SBA are better than what the market would provide.

To address SBA's Office of Inspector General as well as internal policy concerns, SBA has adjusted the credit elsewhere test to incorporate standard market practices and mirror the approach used by most lenders in making credit decisions. In October 2007, these changes were incorporated into our Disaster Standard Operating Procedure (50 30 6), which is publicly available for review on SBA's website. This approach examines the applicant's cash flow to assess repayment ability, assets available to secure the loan, and, in the case of homeowners, the applicant's credit history. The test compares the applicant's net assets to the amount of uncompensated loss and the applicant's available cash flow to repay the loan at market rates. For example, under this test, a business applicant with an uncompensated loss of $2 million would have to have an adjusted net worth of more than $8 million to be determined to have credit available elsewhere. These improved standards ensure the test is a reasonable measure of an applicant's ability to obtain credit from non-Federal sources at reasonable terms and rates.

I fully understand your concerns on this issue. I believe that SBA's decision to re-examine the disaster loans to businesses made at the credit elsewhere rate will alleviate some of the concerns you have expressed. I hope you share my opinion that SBA has significantly improved its disaster operations and responsiveness. The turn-around times for loan processing have improved significantly, and the Agency is processing loans faster than our set goal. Our dedicated personnel in Iowa, many of whom opened our Disaster Recovery Centers within an hour of the Presidential Declaration in Iowa, are still on the ground providing assistance to businesses and homeowners as they recover from the floods. I hope that we can continue to work together to ensure Iowans and Midwesterners receive the assistance they need to recover from these floods.

Sincerely,

Sandy K. Baruah
Acting Administrator