

Testimony of Eric Zarnikow
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Chairwoman Bean, and members of the Committee, thank you for inviting me to testify about the U.S. Small Business Administration's FY 2009 budget for Capital Access programs.

I am Eric Zarnikow, Associate Administrator for Capital Access. I joined the Administration in December of last year, bringing more than 25 years of private sector business experience in accounting, finance and risk management. I am leading the Capital Access team in the many exciting initiatives and improvements planned for 2008. The budget request for FY 2009 reflects the President's commitment to America's small businesses and supports Administrator Preston's Reform Agenda to improve the Agency's services and make our programs more customer-driven.

Since 2001, SBA programs have continued to grow, while we have worked to streamline processes, make technological improvements and develop tools that increase our effectiveness. SBA continues to reach more small businesses through our business loan programs – and doing so while seeking to minimize the cost to the taxpayer. In FY 2001, the loan programs served about 42,000 small business borrowers. In FY 2007, the SBA provided funding to 89,400 small business borrowers in the 7(a) and 504 loan programs.

Through SBA's loan program and the delegated authority provided to participating banks, SBA has provided access to capital to small businesses and entrepreneurs who have had difficulty obtaining capital elsewhere. In FY 2007, SBA was able to reduce the cost to lenders of participating in SBA programs by increasing the efficiency of our processes and encouraging more lenders to make greater use of the capital access programs. The SBA completed all centralization of 7(a) and 504 loan processing functions, allowing for a more streamlined process that provides lenders with a better response time and improved services.

Over \$300 billion of U.S. exports -- about 30% of total U.S. exports -- are originated by small business. These exports generate thousands of jobs and billions of dollars of income for small business. International trade also exposes American small businesses to new ways of doing business- from both a technology and management perspective- all of which make them more competitive not only overseas, but domestically as well. In a rapidly globalizing economy, international trade is the best way for small business to participate in an expanding world economy. Where the U.S. has more free access to foreign markets, reducing the costs of doing business abroad, more small businesses can become global players and grow at a much faster rate. SBA's International Trade Program provided 2,968 loan guarantees to support small business exporters and provided counseling and training to lenders and borrowers. The SBA has

aligned staff at U.S. Export Assistance Centers throughout the country and works closely with the Department of Commerce to provide services to small businesses seeking export assistance.

I am excited to be a part of Administrator Preston's management team. Our Capital Access team looks forward to continuing to work with the Committee to continue to improve access to our services by the small business community, through process improvements that are customer-focused, and outcome-driven. Our goal is to implement improvements that are employee enabled, efficient, transparent and effective. We are also focused on lender outreach and retention. We will continue to ensure capital access products and services are accessible to entrepreneurs in the nation's most underserved markets – those with higher rates of unemployment and poverty and lower rates of economic progress.

Highlights of the Budget Request

The President's FY 2009 proposal will support a total of \$28 billion in lending authority for small business financing, which represents a 37% percent increase over actual business lending for FY 2007, through the 7(a), 504, Microloan and SBIC debenture programs. The proposal requests authorizations of \$17.5 billion for the 7(a) program, \$7.5 billion for the 504 program, \$3.0 billion for the SBIC debenture program, and \$25 million for the Microloan program.

The 7(a), 504 and SBIC program levels build on the continuing success SBA has achieved in its loan programs over the past five years. In 2007, we served more small businesses than ever before. In our two major loan programs, the numbers of gross approvals has increased by 99%, from 50,233 in FY 2002 to over 110,000 loans in FY 2007. 7(a) lending to minority-owned small businesses increased from 13,485 loans in FY 2002 to 34,114 loans in FY 2007. Women-owned business 7(a) lending experienced similar growth, from 10,364 loans in FY 2002 to 22,832 loans in FY 2007. These record level lending numbers are possible, in part, because of the zero subsidy policy that was adopted at the beginning of FY 2005. A recent Urban Institute study found that loans under the 7(a) and 504 programs were more likely to go to minority-owned, women-owned, and start-up businesses as compared to conventional small business loans. Moreover, the study shows that both the 7(a) and 504 programs are meeting demand among creditworthy start-up and minority-owned firms that meet credit elsewhere requirements.

In FY 2007 more than 2,000 small businesses benefited from over \$707 million in SBIC investments. This SBA program increases the availability of venture capital to small businesses. SBA is working to increase our outreach efforts by participating in a number of forums to heighten the visibility of the SBIC program within all market segments.

The zero subsidy policy in the 7(a), 504 and SBIC programs has allowed the Agency to provide record levels of lending without the need for taxpayer-provided credit

subsidy appropriations, while maintaining fee rates consistent with historical levels. This policy has provided certainty and stability for the 7(a) loan program, which both borrowers and lenders agree is crucial for this widely-used program, while reducing taxpayer costs.

Effectively managing agency resources devoted to SBA's lending activity is another key priority. Many improvements have been made over the past several years by centralizing lending functions. We have centralized 7(a) loan guaranty purchase and liquidation functions as well as 504 loan processing. As a result, 7(a) loan liquidations cost nearly \$17 million less in FY 2007 than in FY 2003 even while our portfolio has grown markedly. Centralization allows for more consistent application of SBA's policies and procedures. It also allows the Agency to better monitor and manage its performance metrics.

As we continue to grow the loan portfolio, the need to provide sufficient infrastructure to manage our risk is more important than ever before. As such, we want to continue to strengthen and support the lender oversight and risk management functions of the Agency. To this end, SBA has increased staffing in those areas and has instituted additional measures to improve oversight. SBA has increased its on-site review of lenders from 55 in 2006 to 80 in 2007 and we currently plan to review over 200 in FY 2008. We have also made improvements to our lender portal that is a key oversight tool we use to monitor the portfolio and focus our efforts in the Office of Credit Risk Management. Lenders are provided access to the portal to receive information about the quality of their portfolio compared to their peers. These measures provide lenders feedback they need to proactively improve their SBA lending and program compliance. The measures also assist SBA in identifying those lenders that present the most risk to the SBA portfolio.

In addition, we are pursuing several measures to minimize the potential for fraud in our 7(a) and 504 loan programs. The Office of Credit Risk Management is looking at ways to leverage data analysis techniques to identify portfolio trends that may be indicators of potential fraud. Data developed from this effort will be referred to OIG for further investigation. Further, the Office of Capital Access is meeting with fraud experts in both the private and public sectors and with federal financial regulators to explore how SBA can further improve its fraud detection capabilities.

Despite record growth in 2007, there is a decline in the SBA year to date number of approvals for FY 2008. We have taken notice of this and are working with lenders and small businesses to ensure that we continue to meet the needs of the small business community. Since joining SBA I have met with lenders in New York, Atlanta and Denver. This morning SBA held a roundtable at the White House with lenders and Senior Administration officials. Meetings have been scheduled in another 6 cities around the country. Additionally, we have provided lenders with new loan products to help them reach specific sectors of the small business community and will continue to work with lenders to find ways to better serve small businesses.

Earlier this year the agency launched the pilot of the Rural Lender Advantage Initiative as a way to work with community lenders that are key to providing lending to economically distressed rural areas. This initiative simplifies application procedures and expands assistance to banks that do not regularly work with SBA.

Another product that we are very proud of is the Patriot Express Loan initiative. This product of our 7(a) program provides capital to veterans, members of the National Guard and Reserve and their spouses. This initiative was launched in June 2007 and almost \$86 million have been provided to small businesses and entrepreneurs. This product provides loans up to \$500,000 that can be used for most business purposes, including startup, expansion, equipment purchases, working capital, inventory or business-occupied real estate purchases. This new product offers support to military families by offering expedited approvals and a lower interest rate than other SBA financing options.

To expand capital to certain sectors of our economy in underserved communities, the Agency has also proposed a change to zero subsidy for our Microloan program. By changing the rate at which intermediaries borrow from the SBA from 3.77% (below the government's cost of funds) to 5.92% (1% above the government's cost), intermediaries will continue to receive a better-than-market rate of interest and SBA will be able to offer more loans to eligible intermediaries. This is particularly beneficial for businesses in those markets that can be reached best through microlenders.

The Agency is also seeking to vastly expand the number of outlets providing training to Microlenders by utilizing our technical assistance resource partners in 950 locations throughout the country, including the Small Business Development Centers and Women's Business Centers. By shifting Microloan technical assistance to our extensive network of existing resource partners and with the rollout of additional online technical assistance, SBA has the potential of tripling the potential outlets for microenterprise lending.

Conclusion

In conclusion, FY 2007 was a year of significant accomplishment for SBA's Capital Access Programs, and with this budget request, we look forward to continuing to build on this success. Today, SBA is helping more small businesses meet their financing needs than ever before.

Thank you for your time today. I would be happy to answer any questions.