

Mission Lenders Working Group

February 26, 2016

Mr. Grady Hedgespeth
Director
Office of Economic Opportunity
U.S. Small Business Administration
409 Third Street, SW
Washington, DC 20416

Re: SBA docket number SBA-2015-0013

Dear Mr. Hedgespeth:

I write on behalf of the Mission Lenders Working Group (the ML Working Group) with comments on the Notice issued by the Small Business Administration (SBA) on December 28th, 2015 announcing the extension of and changes to SBA's Community Advantage (CA) loan guarantee pilot. In addition to commenting on specific changes made in the Notice and the accompanying CA Participant Guide 4.0, our letter includes several recommendations aimed at enabling CA lenders to more effectively and efficiently address the needs of small businesses in underserved markets and furthering the goals of the CA pilot.

The ML Working Group was organized in 2015 by a group of CA lenders, including SBA Certified Development Companies (CDCs), SBA Microloan Intermediaries, and Treasury certified Community Development Financial Institutions (CDFIs), with a shared interest in developing a strong and sustainable CA loan guarantee program. The ML Working Group provides a forum through which lenders can network, share questions and/or concerns, discuss program and policy issues, and collaborate as CA lenders working to increase access to credit for small business owners in underserved areas.

At present 15 CA Lenders are active in the ML Working Group and these lenders are responsible for more than 36 percent of the CA loans made to date, measured in both dollars and number of loans. Members of the ML Working Group appreciate the opportunity to comment on the CA pilot, to identify what is working well and offer recommendations on how the program could be strengthened. We hope the insights shared in this letter are helpful and would welcome the opportunity to discuss the comments and experiences of CA lenders with you and your colleagues in the SBA's Office of Economic Opportunity.

I. Comments on SBA Notice 2015-0013 and Changes to the CA Participant Guide

The following comments relate directly to the program changes and clarifications identified in SBA Notice 2015-0013 and included in the CA Participant Guide 4.0 released on December 28, 2015.

- 1. The ML Working Group supports the extension of the CA Pilot through March 31, 2020 and further recommends that SBA institutionalize the ability of experienced mission lenders to access SBA loan guarantees for loans made to businesses located in underserved markets.** We believe the CA pilot has been a success and we support and applaud the SBA for extending the pilot beyond its previous sunset date of March 15, 2017. That said, we believe the program should be made permanent based on the lessons learned to date by both SBA and its CA lending partners. We encourage SBA to institutionalize the ability of mission lenders to access 7(a) guarantee authority for loans specifically targeting the needs of businesses in underserved markets.
- 2. The ML Working Group supports expansion of CA program eligibility to include SBA Intermediary Lending Pilot Program Intermediaries (ILP Intermediaries) authorized under Section 7(l) of the Small Business Act (15 USC 636(l)).** When launched in 2011, participation in the CA Pilot was limited to three types of mission lender: SBA Microloan Intermediaries; SBA Certified Development Companies (CDCs); and non-federally regulated Community Development Financial Institutions (CDFIs). We support adding ILP intermediaries to the list of eligible lenders as they too are mission oriented lenders. In addition, we urge SBA to request a technical change to the ILP's statute to make SBA Microloan Intermediaries eligible as ILP Intermediaries. The suggested change would further advance efforts to expand access of SBA loan products to underserved markets.
- 3. The ML Working Group supports the requirement that a CA Lender must deploy at least five loans before they can process loan applications under delegated authority.** We support the new 5-loan threshold as opposed to the 10-loan threshold initially required under the pilot because it encourages CA lenders to exercise their delegated authority sooner, which benefits the small business borrowers/customers. At the same time, we believe all new CA lenders, no matter how experienced, should be required to submit full documentation to the SBA's Loan Guaranty Processing Center on the first 5 CA loans deployed to ensure compliance and consistency.
- 4. The ML Working group supports the technical waiver to allow CDC participation in the 7(a) program under the CA pilot.** The CA Participant Guide 4.0 waives the SBA rule (13 CFR 120.820(c)) which prohibits a CDC from investing in or being an affiliate of a lender participating in the 7(a) loan program. By waiving the provision, CDCs or their affiliates can participate in the CA Pilot Program.
- 5. The ML Working Group supports changes to the debt refinancing requirements for CA Lenders.** In order to refinance certain debts, SBA requires a 7(a) lender to demonstrate that the new loan will result in a 10 percent improvement in the small business applicant's cash flow. However, CA Participant Guide 4.0 requires that a CA lender looking to refinance an existing loan must demonstrate that either the new loan will result in a 10 percent improvement in the business's cash flow or that the CA loan exceeds the amount being refinanced by at least \$5,000 or 25 percent, whichever is greater. Changes made to CA rules around debt refinancing will significantly benefit borrowers in underserved markets by allowing CA lenders to be more effectively help business owners who finds themselves trapped in an overpriced on-line loan product or relied on high cost credit card debt for start-up capital. These are common scenarios heard by CA lenders.

6. **The ML Working Group supports expansion of the CA pilot’s definition of an eligible underserved market to include Promise Zones and business owners eligible for SBA Veterans Advantage program. In addition, we recommend the SBA to consider expanding the list of qualified underserved markets to include underserved Minority and Women owned businesses.** When launched in 2011, the CA Pilot’s list of qualified underserved markets included: Low-to-moderate income (LMI) communities; Empowerment Zones and Enterprise Communities; HUBZones; New businesses (firms in business for no more than 2 years); Businesses eligible for Patriot Express, including Veteran-owned businesses; and Firms where more than 50 percent of the full time workforce is low-income or resides in an LMI census tracts. CA Participant Guide 4.0 expands the list of qualified markets to include designated Promise Zones and business owners eligible for an SBA Veterans Advantage loan. Some of the underserved markets targeted by CA are geographic, e.g. LMI communities and HUB Zones, while some of the markets are defined by an underserved population, e.g. new business owners and Veteran owned businesses. The ML Working group suggests that the list of CA underserved markets be expanded to include Minority and Women owned businesses, with particular attention to those businesses located in an underserved geographic market.
7. **The ML Working Group cautions SBA on using the PARRiS analytical review protocol to evaluate CA lenders.** CA Participant Guide 4.0 describes how SBA will use its risk based review and examination protocol, specifically the PARRiS methodology, to evaluate CA lenders. The PARRiS protocol was developed as a tool to assess conventional regulated 7(a) lenders and was not designed to account for or value the unique factors that CA lenders must consider when lending in underserved markets. The ML Working groups suggests that the SBA organize a working group to include some of larger CA lenders as well as the largest combined CA/SBA Microloan Intermediaries to assist in developing or improving an analytical tool that can be used to assess the work of mission lenders.
8. **The ML Working Group supports the requirement that if and when the sale of a CA loan or CA loan portfolio is necessary a concentrated effort must be made to sell the loan or portfolio to a CA Lender in good standing.** Although sales of a CA loan or CA loan portfolio are not permitted as a normal course of business in CA lending, in the event that a sale is necessary as part of a lender's withdrawal from the CA Pilot for example, the revised rule states that a CA Lender must make a concerted effort to sell such loans to a “capable and financially viable CA Lender.” This provision is critically important and we applaud SBA for acknowledging that CA lenders uniquely qualified to understand the type of borrowers/businesses in a mission lender’s portfolio and provide services that a traditional 7(a) lender could, or would, not be able to provide.

II. **Recommendation to Strengthen the CA Loan Guarantee**

The ML Working Group urges the SBA to consider the following recommendations aimed at strengthening the CA loan guarantee and the ability of CA lenders to effectively and efficiently reach, finance and support small businesses in underserved markets. The following recommendations are intended to launch an ongoing conversation between the SBA and members of the ML Working Group as we pursue our common goal: increased access to credit for small businesses in underserved markets.

9. **The ML Working Group recommends that the cap on CA loans be adjusted to allow CA lenders to make larger loans while at the same maintaining the focus of CA Lenders on loans**

of \$250,000 or less. Currently, the amount of a CA loan is capped at \$250,000 and according to recent reports the average CA loan is approximately \$120,000. While the ML Working Group wants to preserve the focus of CA on small businesses in underserved markets and particularly businesses needing smaller loans – lenders would like some flexibility to use CA to make some larger loans. Specifically, CA lenders in the ML Working Group report on the challenges facing businesses needing between \$250,000 and \$500,000. These are viable businesses that are unable to secure the financing they need from a conventional bank, even with the benefit of 7(a), and could benefit greatly from the involvement of a CA Lender. There are very few sources of capital that mission lenders can use to address this financing gap and we encourage the SBA to consider granting CA Lenders the ability to make larger loans while maintaining the focus of CA on smaller loans. While the ML Working Group would like to discuss this issue and possible remedies with SBA, in the meantime we offer two options for consideration. Both are based on existing federal loan programs targeting underserved markets.

Option 1: The amount of a CA loan may not exceed \$500,000 and no more than 25 percent of the loans in a CA Lender’s portfolio can exceed \$250,000. (based on USDA’s Intermediary Relending Program (IRP) regulations).

Option 2: The amount of a CA loan may not exceed \$500,000 and a CA lender must maintain a CA portfolio with an average loan size of not more than \$250,000. (based on SBA Microloan Program statute 7(m)6(B))

10. The ML Working Group recommends waiving fees on CA loans of \$250,000 or less. Currently, there are no fees on SBA loans, including CA loans, of \$150,000 or less and upfront fees on CA loans between \$150,000 and \$250,000 vary depending on loan terms. Under the current system, if a borrower needs \$160,000 instead of \$150,00, the fees on the loan jump from \$0 to \$4,800 in order to borrow an additional \$10,000. We do not want CA rules to discourage a business from borrowing the capital they need to avoid paying the fees that we know can be a barrier for entrepreneurs seeking financing. Recognizing that the mission of CA Lenders is to reach, finance and support businesses in underserved markets by providing loans of up to \$250,000 we urge the SBA to permanently waive the fee on CA loans of \$250,000 or less. If SBA permits CA lenders to make larger loans, as we suggested previously (recommendation #10), the ML Working Group recommends that a fixed upfront fee of 1% to 2% be charged on any CA loan of more than \$250,000. This fee structure would serve to encourage smaller loans while maintaining fees on loans that exceed the CA target of \$250,000.

11. The ML Working Group recommend that a CA Lender be authorized to offer an 85% guarantee on all CA loans of \$250,000 or less. Currently, all 7(a) lenders including CA lenders can offer an 85% guarantee for loans of \$150,000 or less and a 75% guarantee for loans greater than \$150,000 and less than \$250,000. While CA lenders are working with the hardest to serve borrowers, providing credit to those with credit scores down to 120 and they lack the capacity that the larger conventional 7(a) lenders have to cover additional costs or weather losses to their portfolio. In order to encourage and support CA lenders to reach into the communities neglected by larger 7(a) lenders we urge SBA to provide an 85% guarantee on all CA loans of \$250,000 or less. If SBA permits CA lenders to make larger loans in underserved markets, as we suggested previously (recommendation #10), we recommend that a 75% guarantee be provided for any CA loans greater than \$250,000. This proposed guarantee structure recognizes the risk associated with making smaller loans and encourage CA lenders to continue making smaller loans to businesses in underserved markets.

12. The ML Working Group recommends that CA Lenders be allowed to sell participating interests in CA loans. Currently, SBA 7(a) lenders are allowed to sell, or sell a participating interest in, a part of a 7(a) loan to another participating 7(a) lender as long as the Lender gives SBA prior written notice, continues to hold at least 10 percent of the outstanding principal balance of the loan, and continues to hold the note and service the loan. However, CA Participant Guide 4.0 prohibits the sale of participating interests in CA loans. We recommend that the SBA grant CA lenders the same ability as 7(a) lenders to sell participating interests in a loan to another participating CA lender. This allowance would enable CA lenders to increase their level of participation and expand access to capital in underserved markets.

13. The ML Working Group recommends waiving the program user fee for CA Lenders selling on the secondary market. All 7(a) lenders, including CA Lenders, must complete the Secondary Participation Guarantee Agreement (SBA Form 1086) to document the sale of the SBA guarantee portion of a loan on the secondary market. The agreement requires a 7(a) lender to pay a “program user fee” to the SBA “equal to 50% of the portion of the sale price, which is in excess of 110 percent of the principal amount outstanding of the guaranteed portion” of the loan. We urge SBA to waive fee for CA lenders in recognition that financing businesses in underserved markets often require greater attention and technical assistance for which CA lenders are not compensated and waiving the fee would allow CA lenders to recover some of these costs. A waiver would also encourage more CA lenders to utilize the secondary market thus generating additional liquidity for mission lenders.

On behalf of the ML Working Group I want to thank you for the opportunity to share comments on the CA pilot and recommendations aimed at strengthening and sustaining this powerful financing tool. I will follow up with you to discuss next steps and I encourage you to call me or any of the ML Working Group members if you have questions or would like additional information about the comments submitted. We look forward to working with you to advance the goals of this important SBA program.

Sincerely,



Alison Feighan

Attached: list of Mission Lenders Working Group members

MISSION LENDERS WORKING GROUP

Access to Capital for Entrepreneurs, GA

Accion Chicago, IL

Accion East, NY

CDC Small Business, CA

Common Capital, MA

Craft3, WA

Finance Fund Capital Corporation, OH

Kentucky Highlands Investment Corporation, KY

LISC New Markets Support Company, IL

Montana CDC, MT

Mountain West Small Business Finance, UT

Prestamos, AZ

The Support Center, NC

VEDC, CA

Wisconsin Women's Business Initiative Corporation, WI