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Report to the Chairman, Committee on Small Business, House of Representatives

December 1991

SMALL BUSINESS

Financial Condition of SBA's Business Loan Portfolio Is Improving

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Resources, Community, and
Economic Development Division

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The Honorable John J. LaFalce
Chairman, Committee on Small Business
House of Representatives

Dear Mr. Chairman:

This report responds to your request for information on loans made to small businesses under section 7(a) of the Small Business Act, as amended (15 U.S.C. 636). The 7(a) loan program, administered by the Small Business Administration (SBA), was created to provide financial assistance to eligible small business concerns that cannot borrow at reasonable terms from conventional lenders without government assistance.

As agreed with your office, we reviewed the 7(a) portfolio to provide information on

- the number and dollar amounts of direct and guaranteed loans in the portfolio by loan program, as well as some demographic information on loan recipients, including their race, gender, and geographic location;
- the performance of the portfolio as shown by the amount of outstanding principal that is current, in default, or in liquidation; and
- statistics on overall losses to the direct and guaranteed portions of the portfolio, as well as losses incurred by each loan program.

Results in Brief

The financial condition of SBA's 7(a) loan portfolio is improving. Specifically, our analysis shows the following:

- As of September 30, 1991, the 7(a) loan portfolio included almost 90,000 loans valued at over $10.3 billion. Most (89 percent) of the loans were SBA-guaranteed loans, although SBA has made 11 percent of the loans directly. The demographic characteristics of the small business owners represented in the 7(a) portfolio are generally similar to the demographic characteristics of small business owners nationwide.
- The percentage of the portfolio that is nonperforming (in default or liquidation) declined during the past 10 years. At the end of fiscal year 1981, 19 percent of SBA's 7(a) portfolio was nonperforming. The nonperformance rate peaked at 28 percent in 1983 but then declined steadily to 16 percent in 1990.

- Losses in the 7(a) loan portfolio have generally decreased in the past 10 years. In the early 1980s, direct loan losses were as high as 28 percent, and guaranteed loan losses were as high as 19 percent. However, according to SBA data, since the mid-1980s, loan losses have remained below 10 percent for both direct and guaranteed loans.

Background

As part of its mission to help people get into business and stay in business, SBA provides financial assistance to eligible small businesses that could not otherwise borrow at reasonable terms from conventional lenders. The largest of SBA's financial assistance programs is the business loan program, authorized by section 7(a) of the Small Business Act. The 7(a) business loan program consists of one major loan program—general business loans—and a number of smaller, specialized loan programs, the most significant of which are the handicapped assistance, economic opportunity, energy, veterans, and minority business loan programs.

SBA currently provides financial assistance through two types of loans—guaranteed and direct. Guaranteed loans are made and disbursed by private lenders and guaranteed by SBA for varying amounts, depending on the size of the loan, the type of lender processing the loan, and the use of the proceeds. Unlike guaranteed loans, direct loans are not made through a private lender but instead require SBA to provide the actual outlay of funds for the entire loan amount.

SBA has developed three types of programs through which private lenders may make SBA-guaranteed business loans: the regular, certified, and preferred lender programs. Under the regular program, the private lender accepts the loan application, but SBA performs the credit analysis and retains final loan-making authority. The certified and preferred lender programs, introduced in 1979 and 1983, respectively, differ from the regular lender program in that they provide lenders more authority in making loan decisions. Under the certified program, the lender performs the credit analysis and submits it to SBA for review and an expedited approval decision. Under the preferred program, the lender has full authority to provide SBA's guarantee to eligible loan applicants.

Appendix I of this report provides more detailed background information on the 7(a) loan programs.

Overview of the 7(a) Portfolio

Over the past 10 years, the total outstanding principal in the 7(a) portfolio has remained relatively constant at about $10 billion. However, the actual number of loans has decreased by about 34 percent over this same period. While the percentage of guaranteed loans in the portfolio has increased each year, the percentage of direct loans has steadily declined.

At the end of fiscal year 1990, 63 percent of the outstanding principal in the guaranteed portfolio had been lent under the regular lender program. The certified lender program and the preferred lender program accounted for 26 percent and 11 percent, respectively, of the guaranteed portfolio. The interest rates charged under the three lender programs are generally equal.

The demographic characteristics of the small business owners represented in the 7(a) portfolio are generally similar to the demographic characteristics of small business owners nationwide. White borrowers hold about 85 percent of the total 7(a) outstanding principal, while, according to the Bureau of Census, white business owners generate about 96 percent of small business sales and receipts. Minority borrowers hold about 13 percent of outstanding 7(a) principal, which compares favorably with the proportion (about 4 percent) of small business sales and receipts that minorities generate. Women, however, have a smaller representation in the portfolio than they do in national small business statistics, accounting for about 10 percent of outstanding 7(a) principal while generating about 14 percent of small business sales and receipts.

Geographically, the 7(a) portfolio is concentrated in the states with the most small business activity. For example, businesses located in California, Texas, and New York hold about 30 percent of the outstanding 7(a) principal and generate about 29 percent of national small business sales and receipts.

Appendix II provides a more detailed overview of the 7(a) loan portfolio.

The Percentage of Nonperforming Loans Is Declining

Overall, the performance of SBA's 7(a) loan portfolio has improved in the past 10 years. The percentage of loans in default or liquidation rose in the early 1980's, peaking at 27.9 percent in 1983, but has steadily declined since then. At the end of fiscal year 1990, the percentage of loans in default or liquidation was down to 16.0 percent of the portfolio.

Guaranteed loans have performed significantly better than direct loans in the 7(a) portfolio. As of September 30, 1990, 14.6 percent of guaranteed 7(a) loans were in default or liquidation, compared with 29.6 percent of direct 7(a) loans.

Among the three lender programs, the preferred program shows the best performance. At the end of fiscal year 1990, the combined default and liquidation percentages for the preferred, certified, and regular lender programs stood at 6.7 percent, 11.2 percent, and 17.4 percent, respectively.

Loans made under the special loan programs, though comprising only 4 percent of the total portfolio, do not perform as well as general business loans. Loans made to either men or women perform about equally, but payment performance varies significantly according to the race and geographic location of the loan recipient.

Appendix III contains a more detailed discussion of 7 (a) loan performance.

Losses in the 7(a) Loan Portfolio Have Generally Decreased

According to SBA data, losses for loans made under the 7(a) program have decreased over the past 10 years. For direct loans made in 1981, 28 percent of the amount disbursed was eventually written off as a loss. By 1987, this loss rate had declined to 9.7 percent. More recent data tend to indicate continued decreasing loan losses. However, since SBA loans usually do not go into default for about 3 years, loans made since 1987 have not been active long enough to measure their performance definitively. For guaranteed loans made in 1981, 16.9 percent of the amount disbursed was eventually written off as a loss. However, by 1987, only 2.0 percent of the amount disbursed for guaranteed loans was eventually written off as a loss.

Overall, loss rates for regular loans are significantly higher (8.5 percent) than loss rates for certified and preferred loans (2.5 percent and 0.3 percent, respectively).

Losses are significantly lower for loans made under the general business loan program (9 percent) than for loans made under the special loan programs. Of these programs, handicapped assistance loans show the lowest loss rates (about 12 percent), while energy loans show the highest (almost 41 percent). As previously noted, however, the special loan programs combined make up only 4 percent of the 7(a) portfolio.

Appendix IV provides more detailed information on loan losses in the 7(a) portfolio.

To obtain information on the number, dollar amount, and performance of loans in the portfolio, and demographic information on the borrowers, we analyzed data tapes from SBA's automated loan accounting system. The data tapes provide loan information as of September 30, 1990. However, because banks report to SBA on a quarterly basis, the data tape information on guaranteed loans shows actual loan activity as of July 30, 1990. To obtain historical information on the amount of outstanding loan principal and the number of loans for fiscal years 1981 through 1990, we reviewed SBA's Management Information Summary report for the end of each fiscal year. To calculate loan loss rates, we obtained loan disbursement data from SBA's Office of Accounting Operations and data on loan losses from SBA's automated loan accounting system. Appendix V of this report discusses our objectives, scope, and methodology in greater detail.

Because our analysis relied on SBA's automated data, we discussed SBA's policy and procedures for maintaining the agency's data bases with the responsible officials from SBA's Office of Financial Management. We also assessed the reliability of SBA's automated data by testing their accuracy and completeness. On the basis of these tests and assessments, we concluded that the information in SBA's loan accounting data base, while having some limitation, was sufficiently reliable to meet our assignment objectives. Appendix V provides a detailed description of our reliability assessment.

We discussed the information presented in this report with SBA's Assistant Administrator for Financial Assistance and members of his staff, who generally agreed with its contents. We have incorporated their comments where appropriate. However, as requested, we did not obtain written agency comments on a draft of this report. We conducted our review between October 1990 and June 1991 in accordance with generally accepted government auditing standards.

As agreed with your office, unless you publicly announce its contents earlier, we will make no further distribution of this report until 30 days after the date of this letter. At that time, we will send copies to the Administrator, Small Business Administration; the Director, Office of Management and Budget; and other interested parties. Copies will be made available to others upon request.

If you have any questions concerning the matters discussed in this report, please contact me at (202) 275-5525. Major contributors to this report are listed in appendix VI.

Sincerely yours,

John M. Ols, Jr.
Director, Housing and Community
Development Issues

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Abbreviations

CLP	certified lender program
EOL	economic opportunity loans
FDIC	Federal Deposit Insurance Corporation
GAO	General Accounting Office
HAL	handicapped assistance loans
MIS	Management Information Summary
OMB	Office of Management and Budget
PLP	preferred lender program
SBA	Small Business Administration
SIC	standard industrial classification

Background on the 7(a) Portfolio

The Small Business Administration (SBA) is an independent agency created by the Small Business Act to assist, counsel, and serve as an advocate for small businesses. Simply put, the mission of SBA is to help people get into business and stay in business. As part of its mission, SBA provides financial assistance to eligible small business concerns that cannot borrow at reasonable terms from conventional lenders without government help.

Section 7(a) of the Small Business Act authorizes the business loan program, the largest of SBA's financial assistance programs. As of September 30, 1990, the dollars outstanding from this program represented 72.8 percent of all SBA financial assistance. The remaining 27.2 percent of the agency's financial assistance was divided among small business investment company assistance (0.4 percent), disaster loan assistance (13 percent), and development company loans (13.8 percent). This report provides information on the 7(a) business loan program, which consists of one major loan program—general business loans—and a number of smaller, specialized loan programs, the most significant of which are the handicapped assistance, economic opportunity, energy, veterans, and minority business loan programs. The general business loan program accounts for 96 percent of the outstanding principal in the 7(a) portfolio, and the smaller loan programs together account for the remaining 4 percent. In this appendix, a description of the special loan programs and their eligibility requirements follows a discussion of the general business program.

The General Business Loan Program

The general business loan program was created to provide loans to small businesses that are unable to obtain financing from private lenders but can demonstrate an ability to repay loans. To be eligible for funds, a business must be independently owned and operated for profit and qualify as small under SBA's size standard criteria, which vary according to the industry. Applicants may be considered for financial assistance only when there is evidence that the desired credit is not otherwise available on reasonable terms. The money lent through this program is to be used to construct, expand, or convert facilities; purchase building equipment or materials; or serve as working capital.

Types of Loans

Within the general business portfolio, SBA has made three types of loans: guaranteed, direct, and immediate participation. Guaranteed loans are made and disbursed by private lenders and guaranteed by SBA for varying amounts, depending on the size of the loan, the type of lender

processing the loan, and the use of the proceeds. In order to establish that the desired credit is otherwise unavailable, the loan applicant is instructed first to make a "good faith attempt" to secure the needed loan from his or her bank of account. If the bank is unwilling or unable to make the loan directly, an SBA guarantee is then considered. SBA's share of a guaranteed loan may not exceed $750,000 except for international trade loans and pollution control loans, which are authorized by sections 7(a)(16) and 7(a)(12), respectively. Both of these loans have a higher SBA maximum guarantee share—$1,250,000 for international trade loans and $1,000,000 for pollution control loans. If a guaranteed loan remains current until it is either fully paid or canceled, SBA will have no cash outlay on the loan. In fact, SBA will collect additional funds through the 2-percent fee that it charges the lender for guaranteeing the loan. However, if a borrower is delinquent on a loan payment for more than 60 days, the lender can ask SBA to purchase the guaranteed percentage of the unpaid principal and interest. When this guaranteed percentage is purchased, an SBA cash outlay results. After purchase, SBA loan officers work with the borrower, sometimes successfully, to make the loan current. If SBA determines that the borrower will be unable to repay the loan, the SBA loan officer transfers the loan to a liquidation status to settle the debt.

Unlike guaranteed loans, direct and immediate participation loans always require a direct outlay of funds from SBA. These loans are available only to applicants who are able to show a proof of refusal for a guaranteed loan from their bank of account. In cities with a population of under 200,000, a refusal from one lender is sufficient. In cities of more than 200,000 people, the applicant must show refusals from the bank of account and one additional lender. SBA lends the entire amount of a direct loan, which has a legislatively limited maximum size of $350,000. However, SBA has administratively limited the size of direct general business loans to $150,000. For an immediate participation loan, both SBA and a private lender put up a share of the loan. SBA's share of this type of loan cannot exceed the lesser of $150,000 or 75 percent of the loan. It should be noted that SBA has not made any direct or immediate participation general business loans since 1985. SBA continues, however, to make direct loans through the special loan programs described below.

Types of Lender Programs

There are three types of private lender programs used in SBA's business loan guarantee program: the regular, certified, and preferred lender programs. Over 12,000 lenders participate in one or more of these three

programs. The regular lender program accounts for about 63 percent of the outstanding principal in the guaranteed portion of the 7(a) portfolio. All regular lenders must demonstrate a continuing capability to evaluate, process, close, disburse, and service loans authorized to be made by SBA to small businesses. The lenders must evidence good character and be under the supervision and examination of a state or federal regulatory authority. SBA also expects that each of these participating lenders will have adequate financial capacity to disburse funds on loans at the time the loan application is approved by SBA. For regular loans, SBA aims to process applications within 20 calendar days of an application's receipt. When processing a regular guaranteed loan, the SBA loan officer will analyze the applicant's creditworthiness using the data provided by the lender and will then determine independently whether the applicant can repay the loan from the profits of the business. If the loan is approved, a loan guarantee agreement is signed, specifying the percentage of the loan that SBA will guarantee.

SBA's loan guarantee is the percentage of the outstanding loan and accrued interest that SBA will pay to a bank if the loan goes into default. In other words, it is the amount of exposure SBA is willing to risk. For regular lender loans under $155,000, SBA must by statute provide at least a 90-percent guarantee. As a matter of policy, however, SBA currently limits its loan guarantee to no more than 90 percent. For regular lender loans of more than $155,000, SBA may guarantee between 70 and 85 percent, depending on the creditworthiness of the borrower and the use of loan proceeds, which are examined on a case-by-case basis. However, when a loan is so large that a 70-percent guarantee will make SBA's share exceed $750,000, a lower guarantee percentage is negotiated. These limits do not apply when a loan is being used to refinance a debt.

When a guaranteed loan made under any type of lender program is used to refinance a debt, SBA may guarantee no more than 80 percent. When only part of the loan is used for debt payment and the rest is for other purposes, the permissible guarantee range of the total loan is determined on a prorata percentage basis. The guarantee on the debt payment portion of the proceeds can range from 0 to 80 percent. A lender may not approve any loan that will reduce its own exposure or the exposure of an affiliate. When a loan or any portion of the loan is used to repay or refinance a debt, the lender must certify that its exposure after the loan is made will be equal to or greater than its exposure before the loan.

To streamline its financial assistance delivery system, SBA introduced the certified (CLP) and preferred (PLP) lender programs in 1979 and 1983, respectively. To be eligible, lenders must (1) already be participating in the regular guarantee program, (2) have a successful lending record with SBA, and (3) demonstrate a thorough understanding of the agency's policies and procedures. The creation of these programs continued SBA's transition from its role as a "retailer" of loans to a "wholesaler" of financial assistance to small businesses. That is, SBA placed increased emphasis on meeting the needs of small businesses through guaranteeing loans made by private lenders, while its direct loan program remained unfunded. The certified and preferred programs differ from the regular guarantee program in that they provide lenders more authority in making loan decisions.

Certified lenders receive partial loan-making authority, and SBA usually decides whether to approve a certified loan within 3 days. The SBA loan officer reviews the credit analysis supplied by the lender and bases a loan approval determination solely on the information as presented by the lender. Certified lenders are subject to the same rules as guide the guarantee percentage determinations of regular lenders. If necessary, certified lenders may submit some loans under regular processing procedures. Recent SBA information shows that there are about 640 lenders in the certified program, which provide for about 26 percent of the 7(a) general business loans.

The best performing certified lenders can also participate in the preferred lender program, which grants lenders full authority to provide SBA's guarantee to eligible loan applicants. Lenders are selected on the basis of their historical performance with SBA and their demonstrated knowledge of loan making, processing, and servicing. Under the preferred program, the lender and not SBA is responsible for performing a complete credit analysis and for deciding whether to lend to the applicant. The lender is to be sufficiently familiar with the process to eliminate the need for SBA to reanalyze an applicant's loan package. As with regular and certified loans, SBA's share of a PLP loan cannot exceed $750,000. However, because of the minimal agency oversight given to these lenders, PLP loans receive a lower guarantee percentage than those made in the certified and regular lender programs—a maximum of 80 percent. Consequently, even loans of less than $155,000, which under the regular lender program receive a 90-percent guarantee, receive only an 80-percent guarantee under the preferred loan program. Recent SBA information shows that about 150 lenders participate in the preferred

program. PLP loans constitute about 11 percent of the 7(a) general business loan portfolio. Preferred lenders can also process loans under regular or certified guarantee procedures when (1) eligibility must be determined by SBA, (2) a conflict of interest exists, or (3) some other condition exists that requires SBA approval.

Interest Rates

Calculations of interest rates for the general business loan program depend on the type of loan and type of lender making that loan. As discussed below, for direct loans, SBA uses a rate of interest specified by law. Regular and certified lenders making guaranteed loans can use either a fixed or a variable rate of interest, subject to certain interest rate guidelines. Preferred lenders are not subject to interest rate restrictions.

Specifically, direct loan interest rates are fixed and are based on the cost of money to the federal government. The rate is calculated quarterly by SBA's Administrator and then provided to SBA field offices. The rate used on the individual loans is assigned by the field office on the basis of the rate in effect at the time the loan is approved.

For guaranteed loans, interest rates may be fixed or variable and are negotiated between the borrower and the lender, subject to SBA maximums. According to SBA, currently about 25 percent of the guaranteed loans are made at a fixed rate and 75 percent at a variable rate. For fixed-rate guaranteed loans, a lending institution may not increase the rate of interest as long as the SBA guarantee remains in effect. For both regular and certified lenders, the maximum interest rate that can be charged on a fixed- rate loan is based on the lowest New York prime rate on the date that SBA receives the loan application plus a fixed maximum percentage amount, or "spread," set by SBA. Interest rates for loans with maturities of 7 years or more cannot exceed 2-3/4 percent over the prime rate; interest rates for loans with maturities of less than 7 years cannot exceed 2-1/4 percent over the prime rate.

Although the interest rate on fixed-rate loans never changes, the interest rate on variable-rate loans does and is linked to either the New York prime rate or the SBA optional peg rate. The New York prime rate is published daily in the Wall Street Journal and, according to SBA officials, is the rate used by most lenders. The SBA optional peg rate is generally published by SBA in the Federal Register at the first of each quarter. The SBA rate is an intermediate-term rate based upon the U.S. Treasury's cost of money. Variable-rate loans are adjusted, but not more than

monthly, to reflect changes in the selected base rate. When the loan rate is adjusted, it must always bear a constant relationship to this rate by virtue of a fixed percentage spread, which cannot exceed the maximum set for fixed-rate loans—2-3/4 percent for loans of 7 years or more and 2-1/4 percent for loans of less than 7 years.

Lenders participating in the preferred lender program are not subject to the regulations that guide the regular and certified lenders in determining the interest rate charged. Preferred lenders can base their interest rates on the New York prime rate or on their own prime rate, both of which may fluctuate daily. According to SBA officials, most preferred lenders use the New York prime rate. SBA officials stated that for the preferred lenders that do use their own rate, the competition among lenders ensures that the rates charged are close to the New York prime rate. There is no maximum spread restriction for PLP lenders.

Term of Loan

Maturity periods for SBA loans are determined on the basis of the borrower's repayment ability and use of the proceeds. SBA sets maximum terms that are not to be applied when a loan can reasonably be repaid over a shorter term. According to SBA's standard operating procedures, the term of a loan should not exceed 10 years except when the proceeds of the loan are used to purchase machinery and equipment or to finance the construction of new facilities or the rehabilitation of an existing facility. In these cases, the term may be as long as, but not exceeding, 25 years. In addition, loans for working capital do not normally exceed a 7-year maturity unless such an extension will lower a borrower's monthly payment and improve his or her repayment ability. In these cases, the term still cannot exceed 10 years.

Special Loan Programs Within the 7(a) Portfolio

In addition to the general business loan program, section 7(a) of the Small Business Act contains subsections that authorize a number of specialized loan programs. The most significant of these programs provide handicapped assistance loans, economic opportunity loans, small business energy loans, Vietnam-era and disabled veteran loans, and minority business loans (commonly referred to as 8(a) program loans). As described below, each specialized loan program caters to the needs of particular borrowers or types of businesses. Combined, these programs make up less than 4 percent of the total 7(a) portfolio.

Except where noted, eligibility, term, interest rate, loan size, and processing procedures are the same for these loan programs as for the general business loan program.

Handicapped Assistance Loans (HAL)—This program was established by section 7(a)(10) to help small businesses owned by sheltered workshops that operate in the interest of handicapped individuals or by people with a permanent physical, mental, or emotional impairment. As of September 30, 1990, this program had $94.3 million outstanding in its portfolio, which was 0.9 percent of the total 7(a) portfolio. The program is divided into two subprograms (HAL-1 and HAL-2) that have different eligibility requirements but the same loan conditions.

HAL-1 provides loans to public and private nonprofit sheltered workshops that operate in the interest of handicapped individuals. At least 75 percent of the business operation's work hours must be provided by handicapped individuals. HAL-2 provides loans to profit-making small businesses that are 100-percent owned and operated by handicapped individuals.

Loans from the HAL program are available on both a direct and a guaranteed basis. Interest rates for direct HAL loans are set by law at 3 percent. The rates for guaranteed HAL loans are guided by the same regulations as the rates for regular guaranteed loans.

Economic Opportunity Loans (EOL)—This program was authorized by section 7(a)(11) to establish, preserve, or strengthen small business concerns that are either (1) located in urban or rural areas of high unemployment or low income or (2) owned by low-income individuals. Statistics on areas of severe or persistent unemployment published by the Department of Labor are used to establish eligibility on the basis of unemployment. To establish eligibility on the basis of low income, over 50 percent of the business must be owned by low-income individuals. SBA defines "low income" as an income that is inadequate to provide basic family needs. These loans are available either directly from SBA or through the guarantee program.

At the end of fiscal year 1990, the outstanding principal for the EOL program was $209 million, or 2 percent of the total 7(a) portfolio.

Small Business Energy Loans—Authorized by section 7(a)(12), this program provides funding to small business concerns involved in engineering, manufacturing, distributing, marketing, installing, or servicing

energy conservation measures. Businesses installing or undertaking energy conservation measures in their own plants or offices are not eligible under this program. Loans from this program, previously available on a direct and guaranteed basis, are now available on a guaranteed basis only.

As of September 30, 1990, the energy loan program had $6.6 million outstanding, or 0.1 percent of the total 7(a) portfolio.

Vietnam-Era and Disabled Veterans Loans—This program provides financial assistance to Vietnam-era and disabled veterans. Vietnam-era veterans are defined as those having served in any branch of the military services for a period of at least 180 days, any part of which was between August 5, 1964, and May 7, 1975. Disabled veterans must be at least 30-percent disabled or must have been discharged from the service for disability. To qualify, the eligible veteran must own at least 51 percent of the business and participate in its day-to-day activities. Loans from this program are available on a direct basis only. An individual may receive only one SBA veteran loan. Any subsequent application for an SBA loan must be filed under another loan program for which eligibility is not determined by veteran status.

As of September 30, 1990, the veterans loan program had $58.3 million outstanding, or 0.6 percent of the total 7(a) portfolio.

Minority Business Loans—These loans are authorized under section 7(a)(20) of the Small Business Act but are part of SBA's minority business development program—commonly referred to as the 8(a) program. The loans provide a source of financing for small business firms participating in the 8(a) program, i.e., those firms owned by socially and economically disadvantaged persons. These loans are available on a direct or guaranteed basis.

As of September 30, 1990, the outstanding principal for the minority business program was $2.2 million, or less than one-tenth of 1 percent of the total 7(a) portfolio.

Interest rates for minority business guaranteed loans are the same as for general business guarantees. For direct loans, the rate is 1 percent less than for direct loans in the general business program.

Loan Status

SBA defines loan status in specific terms, which apply for all 7(a) loan programs. Loans are either current, deferred, past due, delinquent, or in liquidation. To be current, a loan payment must be made either on schedule or within 30 days of the due date. A loan payment can be deferred if a borrower is experiencing a repayment problem that is expected to last for only a limited time. A deferment can be received while the loan is current, past due, or delinquent. SBA's past due category applies when a loan payment is between 31 and 60 days overdue and is the only payment that has been missed. Once a loan is overdue for more than 60 days—more than one payment—it is classified as delinquent.

Finally, a loan can be placed in liquidation. Generally, a loan will be transferred into liquidation status when SBA takes over the loan collateral or otherwise enforces collection or when SBA's interest in the collateral may be in jeopardy as a result of any type of insolvency proceedings. A loan account is considered automatically in liquidation when one or more of the following exist:

- Foreclosure action or a law suit has been instituted against the borrower with respect to any collateral of value.
- The borrower has filed a voluntary petition, or an involuntary petition has been filed against the borrower, under the Bankruptcy Act.
- A receiver has been appointed, an assignment for the benefit of creditors has been made, or other legal action has been taken for the purpose of liquidating the collateral.
- All or a valuable part of the collateral has been abandoned by the borrower.

Standard Industrial Classification Codes

SBA classifies every business according to the categories designated in the Office of Management and Budget's standard industrial classification (SIC) manual. The following categories are used in this report and constitute the major divisions of businesses listed in the manual:

- Agriculture, forestry, and fishing;
- Mining;
- Construction;
- Manufacturing;
- Transportation and public utilities;
- Wholesale trade;
- Retail trade;
- Finance, insurance, and real estate;

- Services;
- Public administration; and
- Nonclassified.

SIC codes serve as the basis for SBA's size standards for small businesses. Size standards vary by industry to account for differences in industry structures. In some cases, the size standard is set in terms of the number of company employees; in other cases, the size standard is determined by the average annual gross revenue of the company. For example, size standards for manufacturers are set by the business's number of employees, which can range from 500 to 1,500, depending on the type of manufacturing. For retailers and service businesses, the size standards are determined by revenue. Businesses having revenues of $3.5 million, and in certain cases of up to $14.5 million, may be considered small, depending on the type of product they offer.

Overview of the 7(a) Portfolio

Since 1981, Guaranteed Loans Have Increased As a Percentage of Total Outstanding Principal in the 7(a) Portfolio

For the past 10 years, the total number of outstanding loans in SBA's 7(a) portfolio has steadily decreased until in 1990 the portfolio contained only two-thirds as many loans (95,494) as it did in 1981 (143,686). (See table II.1.) During this downward spiral, the percentage of direct loans in the portfolio decreased from 24 percent of the total to 16 percent. During the same years, although the actual number of guaranteed loans also decreased (from 108,862 to 80,039), the overall percentage of guaranteed loans in the portfolio actually increased from 76 percent to 84 percent.

Despite this decrease in the overall number of loans, as shown in table II.2, the total outstanding principal in the portfolio has slightly increased during this same period from $10.1 billion in 1981 to $10.7 billion in 1990. This increase in total outstanding principal has occurred, despite the drop in actual numbers of loans, largely because SBA raised its guaranteed loan ceiling from $500,000 to $750,000 in August 1988, thereby enabling private lenders to make larger loans with an SBA guarantee.

Table II.1: Total Number of Loans From Fiscal Year 1981 to Fiscal Year 1990

Fiscal year	Total number of loans outstanding	Number of direct loans	Percentage of total portfolio	Number of guaranteed loans	Percentage of total portfolio
1981	143,686	34,824	24.2	108,862	75.8
1982	142,746	34,425	24.1	108,321	75.9
1983	134,733	32,420	24.1	102,313	75.9
1984	129,453	30,694	23.7	98,759	76.3
1985	122,869	28,686	23.3	94,183	76.7
1986	112,130	25,596	22.8	86,534	77.2
1987	104,846	22,065	21.0	82,781	79.0
1988	98,713	19,294	19.5	79,419	80.5
1989	96,201	17,401	18.1	78,800	81.9
1990	95,494[a]	15,455	16.2	80,039	83.8

[a]The total number of loans shown in this table is larger than the total number of loans shown in tables that are based on our analysis of SBA's data tapes. This discrepancy occurs because the source for the total shown above includes not only the number of loans outstanding but also the number of liquid assets outstanding (e.g., notes receivable, collateral purchased accounts, and judgments). See appendix V for a detailed explanation.

Source: GAO's analysis of SBA's Management Information Summary.

Table II.2: Total Outstanding Principal From Fiscal Year 1981 to Fiscal Year 1990

Dollars in millions

Fiscal year	Total outstanding principal[a]	Outstanding principal for direct loans	Percentage of outstanding principal	Outstanding principal for guaranteed loans	Percentage of outstanding principal
1981	$10,140.6	$1,255.2	12.4	$8,885.3	87.6
1982	10,399.2	1,303.7	12.5	9,095.3	87.5
1983	10,143.4	1,277.0	12.6	8,866.4	87.4
1984	10,259.2	1,265.5	12.3	8,993.8	87.7
1985	10,334.7	1,233.5	11.9	9,101.1	88.1
1986	9,702.1	1,122.3	11.6	8,579.8	88.4
1987	9,634.4	986.3	10.2	8,648.1	89.8
1988	9,598.9	888.1	9.3	8,710.7	90.7
1989	10,006.9	818.2	8.2	9,188.8	91.8
1990	10,677.3[b]	753.3	7.1	9,924.0	92.9

[a]Totals may not add because of rounding.

[b]The total outstanding principal shown in this table is larger than the total outstanding principal shown in tables that are based on our analysis of SBA's data tapes. This discrepancy occurs because the source for the total shown above includes not only loan principal but also the value of liquid assets outstanding (e.g., notes receivable, collateral purchased accounts, and judgments). See appendix V for a detailed explanation.

Source: GAO analysis of SBA's Management Information Summary.

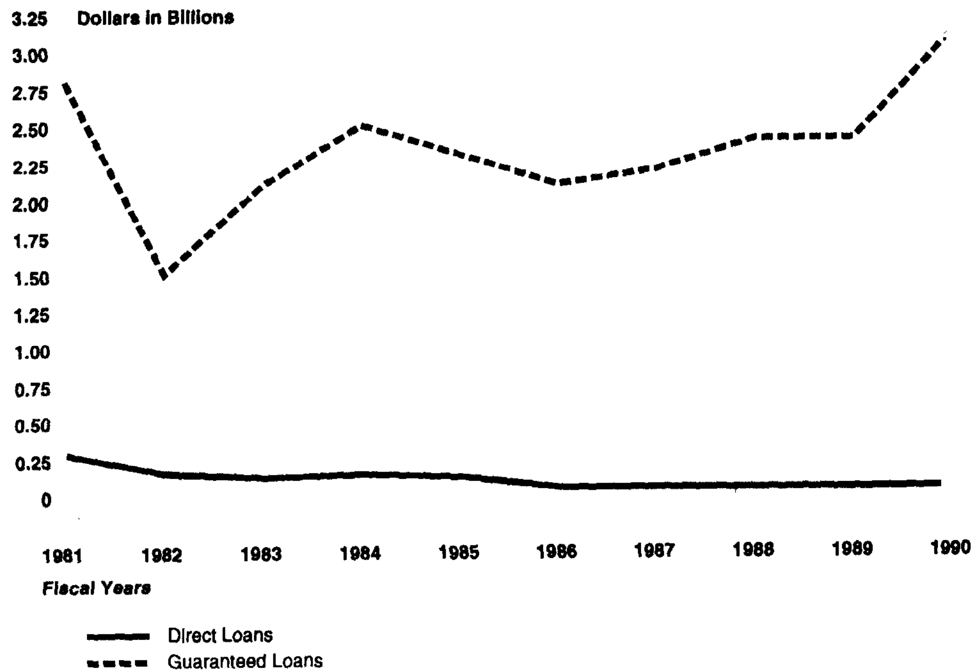
7(a) Lending Levels Have Been Generally Increasing Since 1982

Overall, the amount of funds SBA approved for business loans in 1990 was about the same as it was 10 years ago in 1981, or about $3.1 billion. That level, however, decreased by almost half in 1982—to $1.7 billion. This drop occurred when the then Administration proposed closing SBA. It also coincided with the time when interest rates in general reached an all-time high. According to SBA officials, it was during this period of uncertainty that both lender and borrower interest in SBA loans decreased drastically. However, since 1982, confidence in the agency's continued existence has been restored, and interest rates have stabilized. As a result, the value of loan approvals has increased in almost every year until in 1990 it exceeded the 1981 value (from $3.11 billion in 1981 to $3.14 billion in 1990).

The relative percentage of funds approved for direct and guaranteed loans reflects the agency's increasing emphasis on the guarantee program. The amount approved for guaranteed loans in 1981 was about 91 percent of the total amount, and the remaining funds were approved for direct loans. By 1990, almost 99 percent of the total funds approved for 7(a) loans was designated for the guaranteed portfolio.

Figure II.1 shows the trend in 7(a) loan approvals over the past 10 years.

Figure II.1: Direct and Guaranteed Funds Approved for Lending From FY 1981 to FY 1990



Total Outstanding Principal and Loans in the 7(a) Portfolio as of September 30, 1990

At the end of fiscal year 1990, SBA's 7(a) portfolio had almost 90,000 loans valued at over $10.3 billion outstanding. The dollar value of direct loans in the portfolio is proportionally smaller than that of guaranteed loans, as required by legislative loan ceilings. Direct loans account for over 11 percent of the total number of loans but only 4 percent of the total outstanding principal. The guaranteed portion of the portfolio contains 22 times as much money and 8 times as many loans as the direct portion of the portfolio. As of September 30, 1990, the guaranteed portion of the portfolio included $1.2 billion in loan guarantees that SBA has had to purchase because of borrower default. Table II.3 shows the 7(a) portfolio, categorized by direct loans, guarantees purchased, and guaranteed loans.

Table II.3: Total Outstanding Principal and Number of Loans in SBA's 7(a) Loan Portfolio as of September 30, 1990

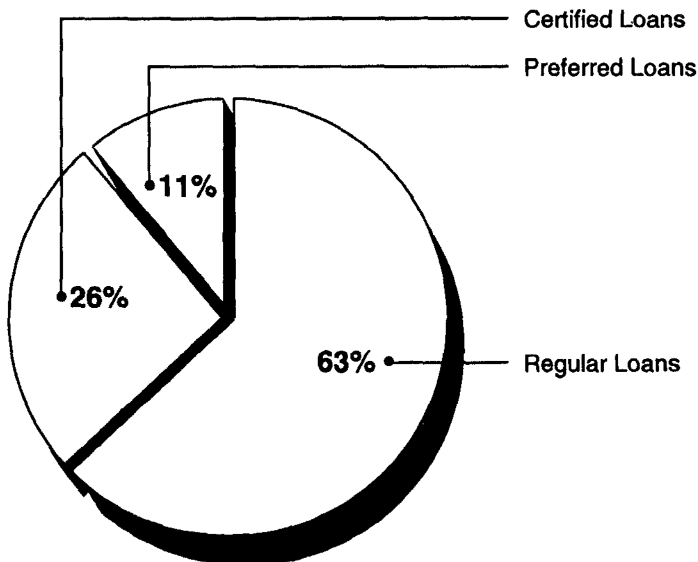
Dollars in millions

Loan	Outstanding principal	Percentage of principal	Number of loans	Percentage of loans
Direct loans	$457.0	4.4	10,057	11.2
Guarantees purchased	1,156.0	11.2	9,921	11.1
Guaranteed loans	8,698.2	84.4	69,789	77.7
Total	**$10,311.2**	**100.0**	**89,767**	**100.0**

Regular Lender Guarantee Loans Account for Almost Two-Thirds of the 7(a) Total Outstanding Principal

As shown in figure II.2, at the end of fiscal year 1990, the regular lender program accounted for 63 percent, or $6.2 billion, of the outstanding principal in the guaranteed portfolio; the certified lender program accounted for 26 percent, or $2.6 billion; and the preferred lender program accounted for the remaining 11 percent, or $1.1 billion. According to SBA, as of September 30, 1990, it had approved 637 lenders for participation in the certified lender program, 154 of which it had also approved for the preferred lender program. Most of the lenders that had participated in the 7(a) loan program (about 11,000 lenders) had been approved for participation in the regular loan program only.

Figure II.2: Percentage of Total Outstanding Principal in the Guaranteed Portfolio by Type of Lender Program as of September 30, 1990



Of the total principal outstanding as of September 30, 1990, under each of the lender programs, 15 percent of the regular loan guarantees ($945 million), 7 percent of the certified loan guarantees ($182 million), and 3 percent of the preferred loan guarantees ($29 million) had been purchased by SBA because of borrower default. According to SBA guidelines based on the extent of SBA's oversight of loan approvals, lenders participating in the preferred lender program are expected to lend to more creditworthy borrowers than certified or regular lenders; regular lenders are expected to lend to the highest risk borrowers. Table II.4 shows the percentage of loan guarantees that SBA has purchased under each of the lender programs.

Table II.4: The Guaranteed Portfolio by Type of Lender Program as of September 30, 1990

Dollars in millions

Lender program	Guaranteed loans	Guarantees purchased	Outstanding principal	Percentage of outstanding principal purchased
Regular	$5,267.9	$945.0	$6,212.9	15.2
Certified	2,400.0	182.2	2,582.2	7.1
Preferred	1,030.3	28.8	1,059.1	2.7
Total amount	**$8,698.2**	**$1,156.0**	**$9,854.2**	

Interest Rates Charged on Guaranteed Loans Are Generally Consistent Among Lenders

Under both the regular and certified lender programs, interest rates have been well below the maximum that SBA allows on guaranteed loans. For the first 4 years of the certified lender program (1979 to 1982), lenders on average charged an interest rate on both regular and certified loans that was lower than the average New York prime rate. During these years, the prime rate soared to an all-time high, averaging 18.87 percent in 1981. For regular program loans made from 1983 to 1990, lenders charged an average of 2.07 percent over the prime rate—less than the 2.25 percent over prime that SBA allows for loans with maturities of less than 7 years and substantially less than the 2.75 percent over prime that SBA allows for loans with maturities of 7 or more years. For the same years, the average interest rate charged on certified loans—2.10 percent over prime—was close to that of regular loans. The interest rates listed in table II.5 reflect the rates charged when the loans were approved.

Preferred loans, which are not subject to SBA interest rate restrictions, have been lent at an average interest rate that was lower than the

average rate charged for certified and regular loans during 4 of the program's 8 years. During these 8 years, preferred loan interest rates averaged 2.01 percent over the New York prime rate, slightly less than the average rate charged for regular and certified loans. SBA officials said that interest rates somewhat depend on the borrower's credit character, and since the preferred program is designed for the more creditworthy borrowers, interest rates for preferred loans would be expected to be slightly lower than for loans in the other programs.

Table II.5: Average Initial Interest Charged per Year on Guaranteed Loans by Type of Lender Program

Year of approval	Average prime rate	Average interest rate for regular lender loans	Average interest rate for CLP loans	Average interest rate for PLP loans[a]
1979	12.67	11.70	12.00	[a]
1980	15.27	13.72	14.70	[a]
1981	18.87	16.34	16.41	[a]
1982	14.86	14.74	14.75	[a]
1983	10.79	12.61	12.74	12.39
1984	12.04	13.45	13.69	13.81
1985	9.93	12.07	12.02	11.72
1986	8.33	10.74	10.67	10.47
1987	8.21	10.64	10.55	10.61
1988	9.32	11.57	11.54	11.60
1989	10.87	12.86	12.88	12.87
1990	10.01	12.15	12.18	12.11

[a]The preferred lender program began in 1983.
Source: GAO analysis of data from SBA and the February 1991 Economic Report of the President

In assessing the reliability of the data base, we estimated that 11.8 percent (±8.5 percent) of the interest rate records were in error. The errors generally occurred because of a lag in data entry for variable-rate loans, whose interest rates constantly fluctuate. SBA estimates that about 70 percent of its loans have variable interest rates. Our analysis was based on the initial interest rate assigned to a loan.

Most SBA 7(a) Funds Are Lent As Long-Term Debt

As shown in table II.6, 93 percent of the outstanding principal in the 7(a) loan portfolio was in long-term loans of 6 years or more. Specifically, the largest percentage of both the direct and guaranteed portfolios was for loans with maturities of 6 to 10 years. For direct loans, 43.6 percent of the portfolio was in the 6- to 10-year category, followed by 30.9 percent for loans with terms of 11 to 15 years. For guaranteed

loans, 37.2 percent of the portfolio had 6- to 10-year maturity periods. The next largest percentage was for guaranteed loans with maturities of over 15 years (35.9 percent). For both direct and guaranteed loans, the smallest percentage of outstanding principal (less than 1 percent) was for loans with a short-term loan period—1 year or less. Generally, neither SBA direct loans nor the guaranteed loans of private lenders are made for such a short term. Otherwise, the borrower would probably qualify for commercial credit without government assistance. In fact, the majority of short-term loans in our data base were actually made for a longer term, but the maturity periods were updated when subsequent action was taken on the loan. Thus, the updated file reflected only the number of months left on the loan.

In assessing the reliability of the data base, we estimated that 19.2 percent (±9.8 percent) of the maturity month records were in error. Most of the errors occurred in liquidated loans where the maturity months had been changed to reflect the remaining months outstanding on the loan instead of the term of the loan when the loan was approved. SBA officials stated that these changes would reflect the effect of deferments granted during the life of the loans.

Table II.6: Total Outstanding Principal in 7(a) Portfolio by Original Term of Loan as of September 30, 1990

Dollars in millions

Term of loan	Direct loans	Guaranteed loans	Outstanding principal[a]	Percentage of total portfolio
Short term (1 year or less)	$0.4	$63.6	$64.1	0.6
Intermediate term (>1 year and <6 years)	13.0	641.8	654.8	6.4
Long term (6 years and over)	443.6	9,148.8	9,592.4	93.0
Total[a]	**$457.0**	**$9,854.2**	**$10,311.2**	**100.0**

[a]Totals may not add because of rounding.

General Business Loans Account for Most of the Total 7(a) Outstanding Principal

The 7(a) portfolio is made up of several programs, the largest of which is the general business loan program, which represents 96 percent, or $9.9 billion, of the portfolio's total outstanding principal. All of the other 7(a) special loan programs combined account for less than 4 percent of the portfolio. The handicapped assistance, veterans, energy, and minority business programs each account for less than 1 percent of the total portfolio.

While SBA makes a large percentage of the special program loans directly, it has not made direct general business loans since 1985. As of September 30, 1990, direct loans comprised about 2 percent, or $198 million, of the general business portfolio. Table II.7 shows the outstanding principal for each of the 7(a) loan programs, as of September 30, 1990.

Table II.7: Total Outstanding Principal in 7(a) Portfolio by Loan Program as of September 30, 1990

Dollars in millions

Program	Direct loans	Guaranteed loans	Outstanding principal[a]	Percentage of total portfolio
General business	$197.6	$9,743.3	$9,940.9	96.4
Economic opportunity	104.0	105.0	209.0	2.0
Handicapped assistance	91.4	2.9	94.3	0.9
Veterans	58.3	[b]	58.3	0.6
Energy	3.4	3.1	6.6	0.1
Minority business	2.2	0[c]	2.2	0
Total amount[a]	**$457.0**	**$9,854.2**	**$10,311.2**	**100.0**

[a]Totals may not add because of rounding.

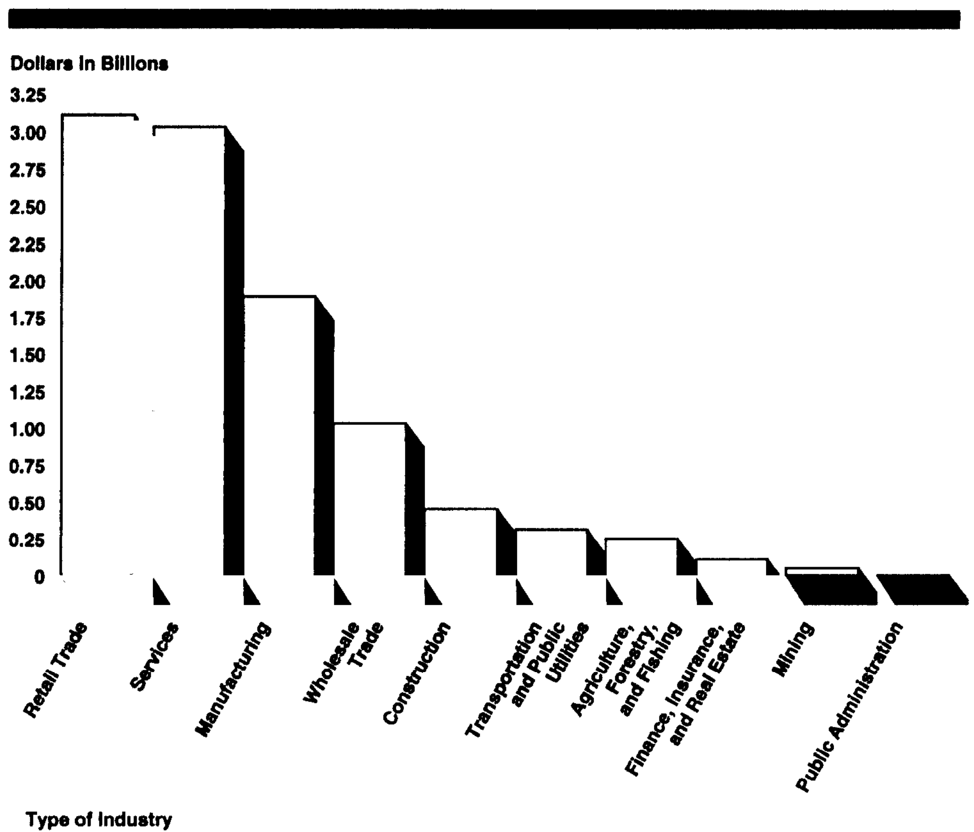
[b]Loans from the veterans program are available on a direct basis only.

[c]There are no guaranteed loans listed for the minority business program because SBA has made all minority business guaranteed loans under the general business program.

Retail Trade and Service Industries Account for Most 7(a) Outstanding Debt

A large percentage—88 percent—of 7(a) money is divided among four types of industries. Specifically, the retail trade and service industries together account for almost 60 percent (30.2 and 29.3 percent, respectively), or $6 billion, of the portfolio's total outstanding principal. In addition, manufacturing and wholesale trade occupy 18 percent ($1.9 billion) and 10 percent ($1 billion) of the 7(a) portfolio, respectively. All other businesses combined account for only 12 percent, or $1.3 billion, of SBA's total outstanding principal as of September 30, 1990. According to the Bureau of Census' most recent figures on small businesses, as of 1987, retail trade industries made up 27.3 percent and service industries 20.9 percent of small business sales and receipts nationally. These were followed by wholesale trade (15.0 percent) and construction businesses (11.6 percent). Manufacturing businesses accounted for 11.4 percent of national small business sales and receipts. Figure II.3 shows the extent to which the various industries are represented in the 7(a) portfolio.

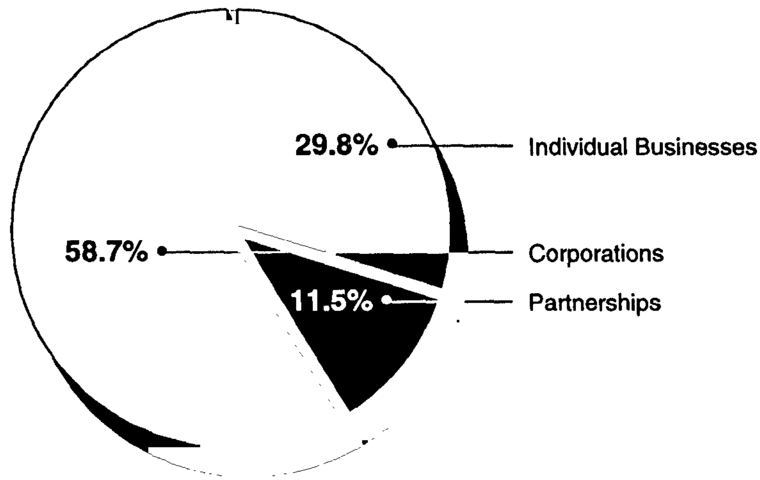
Figure II.3: Outstanding Principal in 7(a) Portfolio by Type of Industry as of September 30, 1990



Most 7(a) Debt Is Owed by Incorporated Businesses

A small business can be organized in one of three ways: as an individual business, a partnership, or a corporation. This designation is made by the potential borrower when filing a loan application. According to SBA, many small businesses incorporate for tax and liability purposes. As shown in figure II.4, the largest percentage, 58.7 percent, or $6.1 billion, of SBA's 7(a) portfolio is lent to small businesses organized as corporations. Businesses owned by individuals account for 29.8 percent of the portfolio ($3.1 billion), and partnerships make up the remaining 11.5 percent ($1.2 billion).

Figure II.4: Percentage of Outstanding Principal in 7(a) Portfolio by Type of Organization as of September 30, 1990



Distribution of 7(a) Debt Is Consistent With Racial Mix of Small Business Owners

The 7(a) portfolio shows a disparate racial composition, but one that is consistent with the most recent Bureau of Census figures on the race of small business owners. White borrowers account for 85 percent of the outstanding principal in the 7(a) portfolio, while, according to the Bureau of Census, white business owners generate about 96 percent of small business sales and receipts. Minority borrowers account for about 13 percent of outstanding 7(a) principal, which compares favorably with the proportion (about 4 percent) of small business sales and receipts that minorities generate. (The race of the borrower cannot be determined for about 2 percent of the outstanding principal.) This comparison also holds for each individual minority group, as tables II.8 and II.9 indicate.

We did not compare the race of people applying for a loan to the race of people who received a loan because SBA does not keep statistics on the race of 7(a) loan applicants.

Table II.9 shows that minorities receive more direct loans than whites as a percentage of the total loans they receive from SBA. As previously noted, direct loans are available only after a guaranteed loan application has been denied by at least one lender. For example, 40 percent of the loans received by black borrowers are from the direct portfolio, and 45

percent of loans to Puerto Rican borrowers are loaned directly. In contrast, white borrowers receive only 7 percent of their loans directly from SBA.

Our analysis of the 7(a) loan programs showed that minorities received a large percentage of their loans from the direct general business portfolio. As of September 30, 1990, black borrowers had received 19.7 percent of their loans from the general business direct portfolio. Of loans for Hispanics, 16.6 percent were direct, and of those for Native Americans, 15.5 percent were direct. In contrast, white borrowers received just 3.7 percent of their loans from the general business direct portfolio. This lending pattern is significant because SBA has not made direct general business loans since 1985. Elimination of funding for this program could therefore have the most impact on minority borrowers.

SBA officials stated that the elimination of the direct portion of the general business loan program will generally make it more difficult for higher risk applicants to receive a loan. The officials also noted that the 8(a) minority business loan program was created in 1989 to take the place of business development grants and, to some extent, will help to fill the void left by the elimination of the direct general business loans. In addition, the economic opportunity loan program was specifically designed to help borrowers from low-income areas. However, our data show that currently the outstanding principal for both of these programs only accounts for 2 percent of the total 7(a) portfolio. Funding for these programs is not expected to increase substantially in the near future.

SBA officials acknowledged that shifting program emphasis from direct lending to guaranteed lending means that some people will be unable to participate in SBA programs. However, according to SBA officials, if an applicant is unable to meet guaranteed lending standards, the increased likelihood of payment problems makes it, in some cases, in the best interest of both SBA and the applicant that no loan be made.

Table II.8: Total Outstanding Principal in 7(a) Portfolio by Race as of September 30, 1990

Dollars in millions

Race	Direct loans	Guaranteed loans	Outstanding principal[a]	Percentage of total portfolio	Percentage of national small business sales and receipts
White	$272.4	$8,525.2	$8,797.6	85.3	96.10
Asian	13.9	500.6	514.5	5.0	1.70
Black	73.1	244.8	317.9	3.1	1.00
Hispanic	48.0	264.8	312.9	3.0	1.20
Undetermined	6.1	146.1	152.2	1.5	[b]
Puerto Rican	35.5	112.4	147.9	1.4	0.10
Amer. Indian	5.6	36.2	41.8	0.4	0.04
Other	1.8	21.6	23.4	0.2	[b]
Eskimo	.7	2.5	3.2	0.0	0.00
Total[a]	**$457.0**	**$9,854.2**	**$10,311.2**	**100.0**	**100.00[c]**

[a]Totals may not add because of rounding.

[b]Percentage cannot be calculated because comparable data do not exist for this group.

[c]Does not include percentages for the "undetermined" and "other" categories because no comparable data exist for these groups.

Source: GAO analysis of data from SBA and the Bureau of Census' 1987 Survey of Minority-Owned Business Enterprises.

Table II.9: Total Number of Loans in 7(a) Portfolio by Race as of September 30, 1990

Race	Direct loans	Guaranteed loans	Total number of loans	Percentage of total number	Percentage of national small businesses
White	5,503	68,899	74,402	82.9	91.1
Black	1,784	2,622	4,406	4.9	3.1
Asian	310	3,186	3,496	3.9	2.6
Hispanic	1,141	2,337	3,478	3.9	2.9
Puerto Rican	1,076	1,296	2,372	2.6	0.2
Undetermined	87	928	1,015	1.1	[a]
Amer. Indian	130	309	439	0.5	0.1
Other	16	113	129	0.1	[a]
Eskimo	10	20	30	0.0	0.0
Total	**10,057**	**79,710**	**89,767**	**100.0**	**100.0[b]**

[a]Percentage cannot be calculated because comparable data do not exist for this group.

[b]Does not include percentage for the "undetermined" and "other" categories because no comparable data exist for these groups.

Source: GAO analysis of data from SBA and the Bureau of Census' 1987 Survey of Minority-Owned Business Enterprises.

Women Have Relatively Less Representation in the 7(a) Portfolio Than They Have in Small Businesses Nationally

The 7(a) gender statistics show that women have a smaller representation in SBA's 7(a) loan portfolio than they do in the statistics on owners of small businesses. As shown in table II.11, about 12 percent of 7(a) loans are made to women and about 87 percent to men. These numbers vary considerably from the Bureau of Census' national figures, which show that women own 30 percent of small businesses nationally. (Because SBA does not keep computerized statistics on the gender of 7(a) loan applicants, we were unable to compare the gender of borrowers with approved loans to the gender of applicants.)

SBA officials stated that women receive fewer SBA loans for the following reasons: (1) Women-owned businesses tend to be smaller in size than other small businesses, and, as such, their owners seek financing from sources other than SBA or commercial lenders. (2) Many women-owned businesses are in the service industry, and, by their nature, have few assets to offer as loan collateral. (3) Most lenders prefer to make larger loans, since they are less labor-intensive and therefore yield more profit. Larger loans tend to be made to larger businesses, which are predominantly male-owned.

Table II.10: Total Outstanding Principal in 7(a) Portfolio by Gender as of September 30, 1990

Dollars in millions

Gender	Direct loans	Guaranteed loans	Outstanding principal[a]	Percentage of total portfolio	Percentage of national small business sales and receipts
Men	$382.6	$8,930.4	$9,313.0	90.3	86.1
Women	70.7	907.8	978.5	9.5	13.9
Missing value	3.8	16.0	19.8	0.2	[a]
Total[b]	**$457.0**	**$9,854.2**	**$10,311.2**	**100.0**	**100.0**

[a]Not applicable.

[b]Totals may not add because of rounding.

Source: GAO analysis of data from SBA and the Bureau of Census' 1987 Survey of Women-Owned Businesses.

Table II.11: Total Number of Loans in 7(a) Portfolio by Gender as of September 30, 1990

Gender	Direct loans	Guaranteed loans	Total number of loans	Percentage of total number	Percentage of national small businesses
Men	7,788	70,251	78,039	86.9	70.0
Women	2,025	9,135	11,160	12.4	30.0
Missing value	244	324	568	0.6	[a]
Total	**10,057**	**79,710**	**89,767**	**100.0**	**100.0**

[a]Not applicable.

Source: GAO analysis of data from SBA and the Bureau of Census' 1987 Survey of Women-Owned Businesses.

7(a) Debt Is Concentrated in States With the Most Small Business Activity

SBA has some loan activity in every state; however, a significant percentage of the outstanding principal is concentrated in a few states. Businesses located in California, Texas, and New York make up 30 percent of SBA's 7(a) loan activity. This concentration of SBA lending corresponds to small business activity. The Bureau of Census reports that businesses in California, New York, and Pennsylvania have the highest small business sales and receipts and account for 28.6 percent of the national total. The state of Texas is fourth in small business sales and receipts, making up 5.8 percent of the national total.

The Bureau of Census also reports that small businesses in Wyoming have the lowest sales and receipts nationally, followed by North Dakota and Delaware. Within the 7(a) portfolio, Delaware receives the fewest SBA dollars, followed by the District of Columbia and then Hawaii. Combined, these three areas make up less than 1 percent of the total 7(a) portfolio.

Table II.12 shows the states with the highest and lowest representation in the 7(a) portfolio and figure II.5 shows how all states are ranked by amount of 7(a) debt. Table II.13 contains a detailed listing of the amount of outstanding 7(a) loan principal for each state.

Table II.12: States With the Highest and Lowest Percentages of 7(a) Outstanding Principal as of September 30, 1990

Dollars in millions

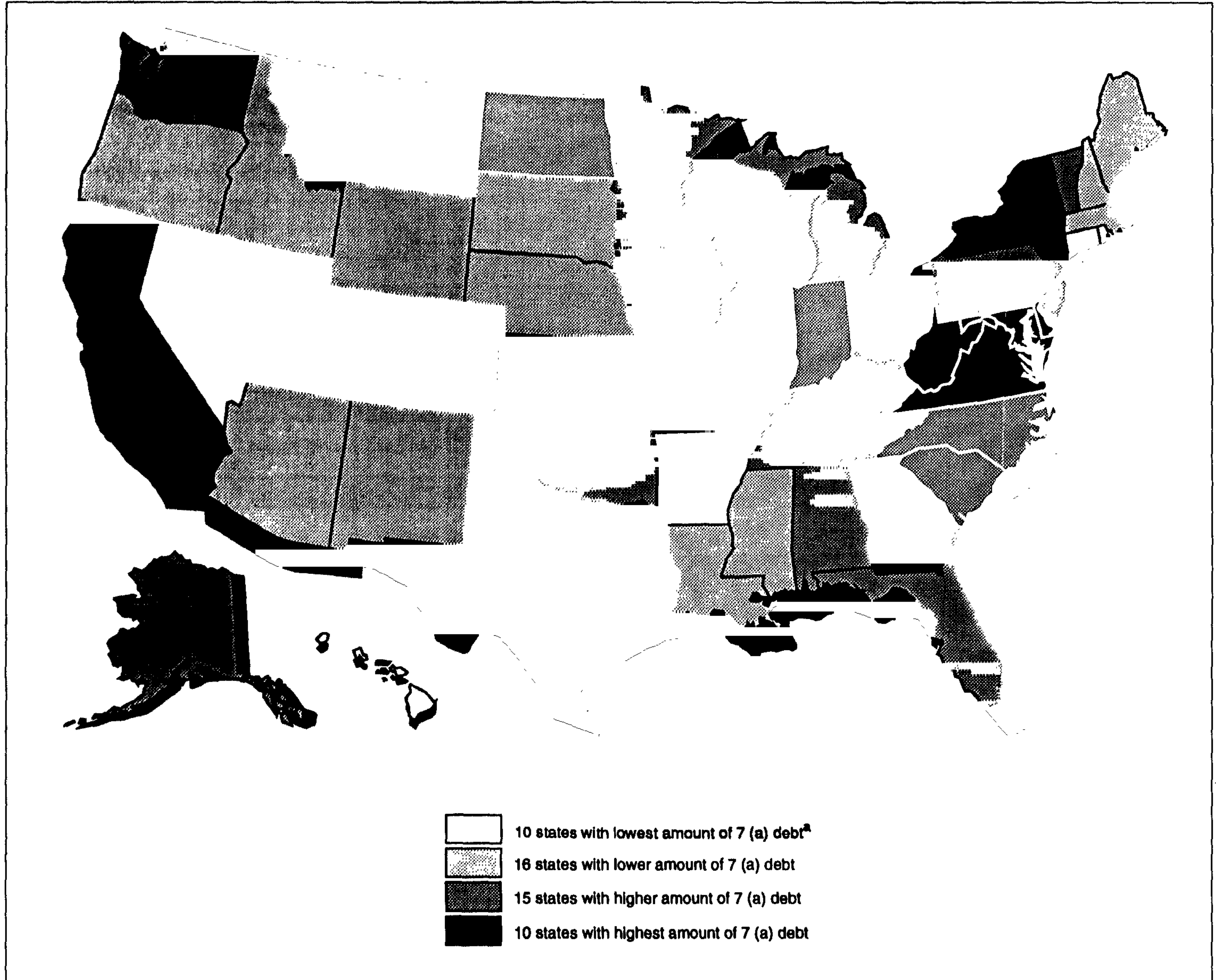
State	Outstanding principal	Percentage of total portfolio	Percentage of national small business sales and receipts
The ten highest:			
California	$1,801.4	17.5	12.4
Texas	809.5	7.9	5.8
New York	525.9	5.1	10.4
Georgia	512.7	5.0	2.4
Wisconsin	394.6	3.8	1.6
Illinois	354.2	3.4	5.0
Missouri	280.6	2.7	1.9
Montana	248.4	2.4	0.3
Ohio	248.3	2.4	3.6
Kansas	241.0	2.3	0.9
Total[a]	**$5,416.5**	**52.5**	**44.3**

State	Outstanding principal	Percentage of total portfolio	Percentage of national small business sales and receipts
The ten lowest:			
Delaware	$8.0	0.1	0.2
District of Columbia	9.9	0.1	0.3
Hawaii	26.1	0.3	0.3
Rhode Island	37.7	0.4	0.5
Nevada	45.9	0.4	0.5
West Virginia	48.9	0.5	0.4
Maryland	56.0	0.5	2.1
Connecticut	56.8	0.6	1.8
Arkansas	57.8	0.6	0.7
Virginia	61.0	0.6	2.1
Total[a]	**$408.3**	**4.1**	**8.9**

[a]Totals may not add because of rounding.

Source: GAO analysis of data from SBA and the Bureau of Census' 1987 Economic Census Report.

Figure II.5: States Ranked by Amount of 7(a) Debt, as of September 30, 1990.



[a]The District of Columbia is treated as a state and is included in this category.
Source: GAO presentation of SBA and Bureau of Census data.

Table II.13: Total Outstanding Principal in 7(a) Portfolio by State and Territory as of September 30, 1990

Dollars in millions

State	Direct loans	Guaranteed loans	Total outstanding principal	Percentage of total portfolio	Percentage of national small business sales and receipts
Alabama (25)	$11.2	$125.0	$136.2	1.3	1.3
Alaska (16)	8.3	188.9	197.2	1.9	0.2
Arizona (26)	5.3	126.2	131.5	1.3	1.1
Arkansas (43)	6.7	51.0	57.8	0.6	0.7
California (1)	43.9	1,757.5	1,801.4	17.5	12.4
Colorado (19)	7.1	175.8	182.9	1.8	1.4
Connecticut (44)	6.9	49.9	56.8	0.6	1.8
Delaware (51)	0.3	7.7	8.0	0.1	0.2
District of Columbia (50)	2.1	7.9	9.9	0.1	0.3
Florida (11)	9.5	222.4	231.9	2.2	5.0
Georgia (4)	12.6	500.1	512.7	5.0	2.4
Hawaii (49)	1.5	24.6	26.1	0.3	0.3
Idaho (32)	4.4	94.2	98.5	1.0	0.3
Illinois (6)	22.7	331.5	354.2	3.4	5.0
Indiana (30)	7.0	104.8	111.9	1.1	2.5
Iowa (13)	4.2	225.4	229.7	2.2	0.9
Kansas (10)	6.6	234.5	241.0	2.3	0.9
Kentucky (21)	7.6	156.7	164.3	1.6	1.1
Louisiana (31)	5.5	95.3	100.8	1.0	1.1
Maine (39)	1.4	80.7	82.0	0.8	0.5
Maryland (45)	10.4	45.6	56.0	0.5	2.1
Massachusetts (29)	9.7	105.5	115.3	1.1	3.3
Michigan (20)	10.9	164.7	175.6	1.7	3.2
Minnesota (17)	6.1	182.6	188.7	1.8	1.7
Mississippi (41)	11.6	58.9	70.5	0.7	0.7
Missouri (7)	9.5	271.0	280.6	2.7	1.9
Montana (8)	2.8	245.6	248.4	2.4	0.3
Nebraska (34)	1.6	94.2	95.8	0.9	0.6
Nevada (47)	1.6	44.3	45.9	0.4	0.5
New Hampshire (37)	2.0	83.9	85.9	0.8	0.7

(continued)

State	Direct loans	Guaranteed loans	Total outstanding principal	Percentage of total portfolio	Percentage of national small business sales and receipts
New Jersey (22)	8.5	150.7	159.2	1.5	4.7
New Mexico (27)	3.0	120.8	123.8	1.2	0.4
New York (3)	23.7	502.3	525.9	5.1	10.4
North Carolina (33)	7.9	90.0	97.9	0.9	2.3
North Dakota (40)	2.0	70.5	72.5	0.7	0.2
Ohio (9)	18.5	229.8	248.3	2.4	3.6
Oklahoma (24)	3.8	134.6	138.4	1.3	1.0
Oregon (35)	5.1	85.4	90.5	0.9	1.1
Pennsylvania (15)	10.1	191.8	202.0	2.0	5.8
Rhode Island (48)	3.3	34.4	37.7	0.4	0.5
South Carolina (38)	6.9	77.4	84.3	0.8	0.9
South Dakota (28)	5.8	111.5	117.3	1.1	0.3
Tennessee (14)	5.6	203.1	208.7	2.0	1.7
Texas (2)	40.3	769.2	809.5	7.9	5.8
Utah (23)	1.9	150.2	152.1	1.5	0.5
Vermont (18)	1.0	182.7	183.7	1.8	0.3
Virginia (42)	7.5	53.5	61.0	0.6	2.1
Washington (12)	7.2	224.5	231.7	2.2	1.8
West Virginia (46)	1.4	47.6	48.9	0.5	0.4
Wisconsin (5)	10.5	384.1	394.6	3.8	1.6
Wyoming (36)	1.4	85.4	86.7	0.8	0.2
Territories[a]	40.4	97.7	138.2	1.3	[b]
Missing Value	0.2	0.8	0.9		
Total amount	**$457.0**	**$9,854.2**	**$10,311.2**	**100.0**	**100.0**

Note: The number in parentheses ranks each state according to the size of its 7(a) debt. For example, California ranks first, with the largest 7(a) debt ($1.8 billion).

[a]Includes American Samoa, Guam, Puerto Rico, and Virgin Islands.

[b]Not applicable.

Source: GAO analysis of SBA data and the Bureau of Census' 1987 Economic Census Report.

Performance of the 7(a) Portfolio

Overall, the Performance of the 7(a) Portfolio Has Improved in the Past 10 Years

Overall, the performance of SBA's 7(a) loan portfolio has improved in the past 10 years. The default percentage, which we have calculated using the number of loans that are at least one payment late but not yet in liquidation, rose from 9.5 percent in 1981 to 12.4 percent in 1982 and then dropped steadily until it reached 5.7 percent in 1990. The liquidation percentage followed a similar pattern. In 1981, $1 billion, or 10 percent, of the 7(a) loan money was in liquidation. By 1985, that figure had risen to 17 percent ($1.7 billion), and then it steadily decreased until, by the end of fiscal year 1990, $1.1 billion, or 10.3 percent, of the portfolio was in liquidation.

SBA officials attribute the improvement in the portfolio's performance to the agency's revised loan-making policy, which, beginning in the early 1980s, began to emphasize the quality rather than the quantity of loans. In practice, this emphasis on quality lending has meant that all loan recipients, while still needing a government guarantee or direct assistance, must also have the ability to repay a loan. As part of this ongoing program improvement, SBA is (1) conducting an extensive training program for its loan officers on making sound loans, (2) encouraging stronger servicing efforts from participating lenders, and (3) emphasizing creditworthiness to lenders participating in the agency's guarantee program.

Table III.1 and figure III.1 show the improvement in 7(a) loan performance during the past 10 years.

Table III.1: Performance of Outstanding Principal in 7(a) Portfolio From FY 1981 to FY 1990

Dollars in millions

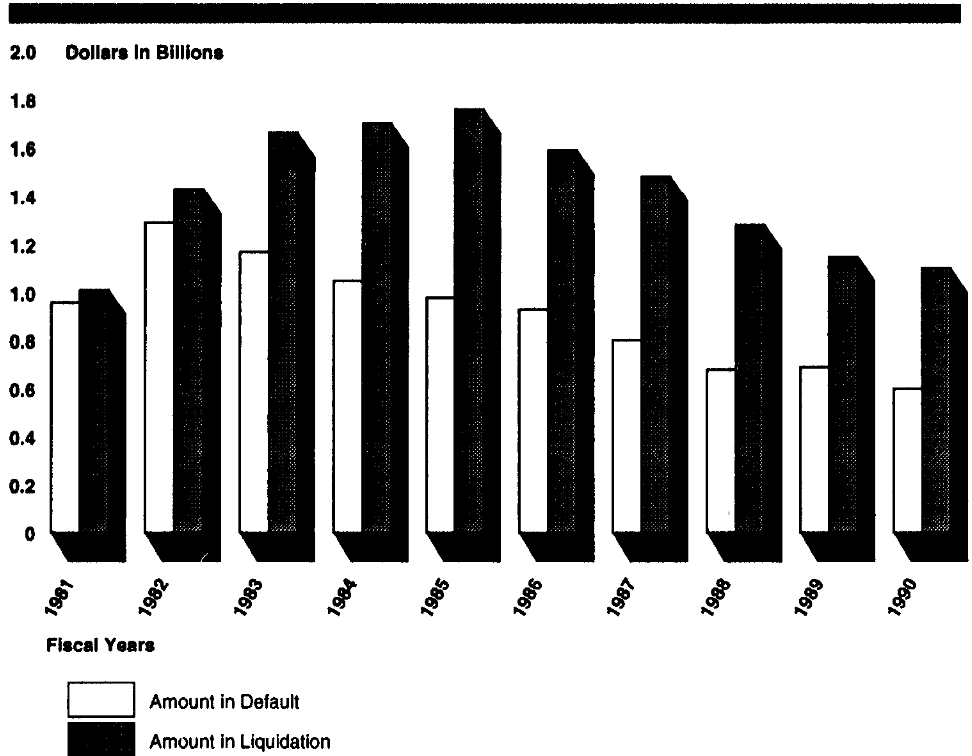
Fiscal year	Amount current/ deferred	Amount in default	Amount in liquidation	Outstanding principal[a]	Default percentage	Liquidation percentage
1981	$8,161.9	$966.1	$1,012.5	$10,140.6	9.5	10.0
1982	7,672.3	1,292.0	1,434.7	10,399.2	12.4	13.8
1983	7,310.4	1,171.2	1,661.8	10,143.4	11.5	16.4
1984	7,511.7	1,051.0	1,696.5	10,259.2	10.2	16.5
1985	7,595.7	978.6	1,760.4	10,334.7	9.5	17.0
1986	7,181.6	929.3	1,591.2	9,702.1	9.6	16.4
1987	7,353.8	796.2	1,484.5	9,634.4	8.3	15.4
1988	7,637.0	682.0	1,279.9	9,598.9	7.1	13.3
1989	8,159.7	693.2	1,154.0	10,006.9	6.9	11.5
1990	8,973.1	603.6	1,100.5	10,677.3[b]	5.7	10.3

[a]Totals may not add because of rounding.

[b]The total outstanding principal shown in this table is larger than the total outstanding principal shown in tables that are based on our analysis of SBA's data tapes. This discrepancy occurs because the source for the total shown above includes not only loan principal but also the value of liquid assets outstanding (e.g., notes receivable, collateral purchased accounts, and judgments). See appendix V for a detailed explanation.

Source: GAO's analysis of data from SBA's Management Information Summary.

Figure III.1: Amount of Outstanding Principal in Default or Liquidation From FY 1981 to FY 1990



Guaranteed Loans Perform Better Than Direct Loans

As shown in table III.2, guaranteed loans generally perform better than direct loans. As of September 30, 1990, the default percentage for guaranteed loans was only half as great (5.3 percent) as the default percentage for direct loans (10.5 percent). An even greater disparity in performance is evident for loans in liquidation—9.3 percent for guaranteed loans compared with 19.1 percent for direct loans. SBA attributes the poor performance of the direct loan portion of the portfolio to the fact that borrowers must have been turned down for a guaranteed loan by at least one and sometimes two (depending on the size of the city where the loan was made) private lenders in order to qualify for a direct loan.

Table III.2: Performance of 7(a) Portfolio by Type of Loan as of September 30, 1990

Dollars in millions

Loan	Amount current or deferred	Amount in default	Amount in liquidation	Outstanding principal[a]	Default percentage	Liquidation percentage
Direct loans	$321.5	$48.1	$87.4	$457.0	10.5	19.1
Guaranteed loans	8,416.0	524.0	914.3	9,854.2	5.3	9.3
Total[a]	**$8,737.5**	**$572.1**	**$1,001.7**	**$10,311.2**		
Overall percentage					5.5	9.7

[a]Totals may not add because of rounding.

Preferred Lender Loans Show the Best Performance In the Guaranteed Portfolio

Analyzing the guaranteed portion of the portfolio by type of loan, we found that, as of September 30, 1990, loans made under the preferred lender program have the best performance. Regular lender loans have the highest default percentage at 6.0 percent. Certified and preferred lender loans have lower default percentages at 4.4 and 3.7 percent, respectively. Certified and preferred loans also have lower liquidation percentages at 6.8 and 3.0 percent, respectively, compared with an 11.4-percent liquidation rate for the regular program.

This distribution of default and liquidation percentages among lender programs is to be expected under current SBA program guidelines. In order to participate in either the certified or the preferred lender program, SBA requires the lender already to have participated successfully in the regular lender program. Consequently, we would expect that the loans of CLP and PLP lenders would perform better than the loans of regular lenders. The especially low default and liquidation percentages of preferred loans are also in keeping with SBA guidelines, which state that PLP loans should be made to more creditworthy borrowers whose loan repayment ability is clear.

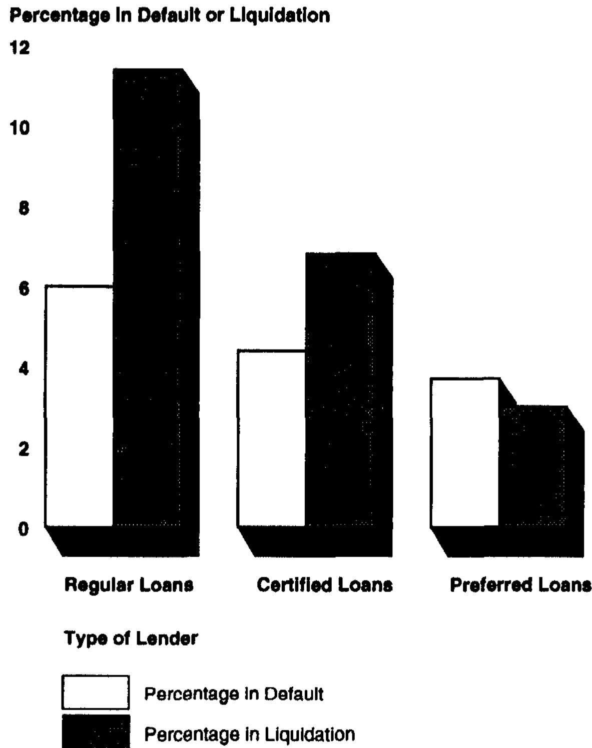
Table III.3: Performance of 7(a) Guaranteed Portfolio by Type of Lender Program as of September 30, 1990

Dollars in millions

Lender program	Amount current or deferred	Amount in default	Amount in liquidation	Outstanding principal[a]	Default percentage	Liquidation percentage
Regular	$5,133.1	$370.6	$707.2	$6,210.9	6.0	11.4
Certified	2,294.1	113.5	174.7	2,582.2	4.4	6.8
Preferred	987.6	39.5	31.9	1,059.1	3.7	3.0
Missing value	1.2	0.4	0.4	2.0		
Total[a]	**$8,416.0**	**$524.0**	**$914.3**	**$9,854.2**		
Percentage of total					5.3	9.3

[a]Totals may not add because of rounding.

Figure III.2: Percentage of Outstanding Principal in Default or Liquidation by Type of Lender Program as of September 30, 1990



Loans With a High SBA Guarantee Percentage Have a Greater Default and Liquidation Percentage

As shown in table III.4, there is a correlation between guarantee percentage and nonperformance percentage. For loans with an 86- to 90-percent SBA guarantee, over 20 percent of the outstanding principal is in default or liquidation, whereas for loans with a 75- to 85-percent SBA guarantee, just over half that percentage is in default or liquidation. SBA officials stated that high default and liquidation percentages frequently accompany high loan guarantee percentages because (1) the lender needed a high guarantee percentage initially to accept a higher risk loan, and (2) with a high guarantee percentage from SBA, the lender has less incentive to keep the loan current.

Loans with an SBA guarantee of less than 75 percent also show a high nonperformance rate—about 16 percent. According to SBA officials, loans guaranteed at less than 75 percent are often refinanced loans, a loan category that tends to involve higher risk.

Table III.4: Performance of Guaranteed Loans by Guarantee Percentage as of September 30, 1990

Dollars in millions

SBA guarantee percentage	Amount current	Amount in default	Amount in liquidation	Outstanding principal[a]	Default percentage	Liquidation percentage
86-90	$2,612.6	$209.2	$453.0	$3,274.7	6.4	13.8
81-85	3,378.3	171.9	249.0	3,799.2	4.5	6.6
75-80	1,845.2	99.5	142.7	2,087.4	4.8	6.8
Less than 75	577.3	43.2	67.5	688.0	6.3	9.8
Total[a]	**$8,413.5**	**$523.7**	**$912.2**	**$9,849.3**		

[a]Totals may not add because of rounding. Totals do not include $4.9 million in outstanding principal that, for special circumstances, SBA guaranteed at over 90 percent.

Loans Made Under the Special Loan Programs Generally Do Not Perform as Well as the General Business Loans

General business loans, which have a 6.2-percent default rate and a 9.3-percent liquidation rate, generally perform better than the special program loans. Within the special programs, handicapped assistance loans are the best performers; 6.3 percent are in default and 4.6 percent in liquidation. The energy loan program is the poorest performer—it has an outstanding principal of less than $6.6 million (55 loans), but of these loans, 36.4 percent are in liquidation and another 10.9 percent are currently in default. The veterans loan program also has poor performance statistics; 14.6 percent of its loans are in default and 15.2 percent in liquidation.

SBA officials explained the poor performance of some of the special programs by stating that most of the principal outstanding in these programs was lent at a time when SBA was leniently applying credit standards to benefit as many people as possible. The officials stated that in recent years SBA has more carefully evaluated credit risk, since loans that perform poorly ultimately benefit neither SBA nor the borrower.

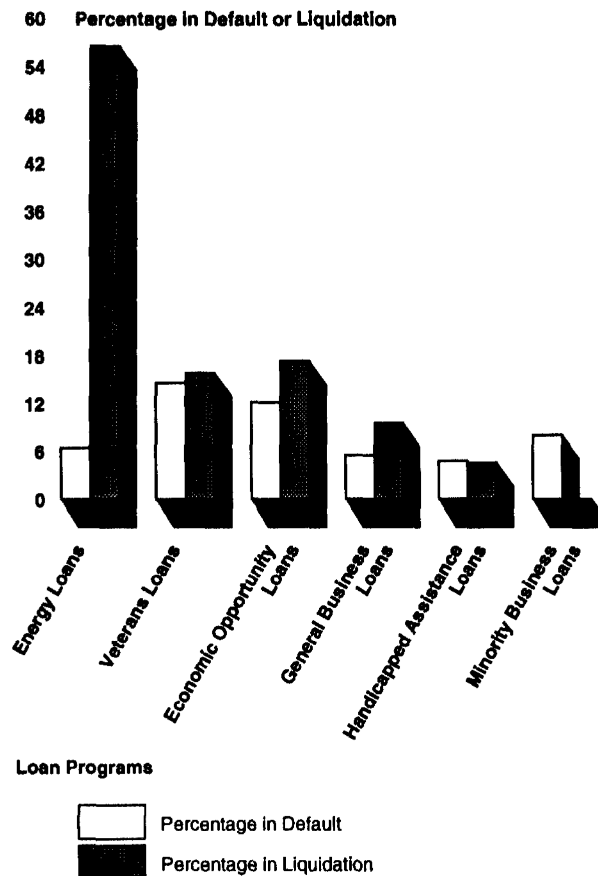
Table III.5: Performance of 7(a) Portfolio by Loan Program as of September 30, 1990

Dollars in millions

Loan program	Outstanding principal	Default percentage	Liquidation percentage	Number of loans	Default percentage	Liquidation percentage
Energy	$6.6	6.4	56.5	55	10.9	36.4
Veterans	58.3	14.6	15.8	975	14.6	15.2
Economic opportunity	209.0	12.1	17.3	4,307	12.2	17.6
General business	9,940.9	5.4	9.6	83,023	6.2	9.3
Handicapped assistance	94.3	4.7	4.5	1,387	6.3	4.6
Minority business	2.2	8.0	0.0	19	10.5	0.0
Total[a]	**$10,311.2**			**89,766**		

[a]Total may not add because of rounding.

Figure III.3: Percentage of Outstanding Principal in Default or Liquidation by Loan Program as of September 30, 1990



Fiscal year 1989 was the first year in which any minority business loans were disbursed. Consequently, these loans have not been active long enough to determine their true performance.

Type of Business Has Little Impact on Loan Performance

Overall, loans made to borrowers from various types of businesses—as designated by the Office of Management and Budget's standard industrial classification code—have similar default and liquidation percentages. Of the four types of businesses with the highest representation in the 7(a) portfolio (retail trade, services, manufacturing, and wholesale trade), the service industry shows the best performance; 88 percent of its outstanding principal is current. Manufacturing businesses have the highest nonperformance percentage at 17.7 percent.

Table III.6: Performance of 7(a) Portfolio by Type of Business as of September 30, 1990

Dollars in millions

Business	Outstanding principal	Default percentage	Liquidation percentage	Nonperformance percentage
Manufacturing	$1,887.0	5.6	12.1	17.7
Retail trade	3,112.1	5.8	10.1	15.9
Wholesale trade	1,031.6	4.7	9.8	14.5
Services	3,025.1	5.2	6.8	12.0
Other	1,255.5	6.2	12.2	18.4
Total[a]	**$10,311.2**			

[a]Total may not add because of rounding.

Performance of 7(a) Portfolio Among Different Types of Business Organizations Is Similar

As shown in table III.7, 7(a) loan nonperformance rates are similar among types of small business organizations. Businesses that have been incorporated have a slightly higher percentage of liquidated funds (11.2 percent) than businesses owned by individuals (7.3 percent) or partnerships (8.5 percent). As of September 30, 1990, the three types of business organizations all had about 5 percent of their outstanding principal in default.

Table III.7: Performance of 7(a) Portfolio by Type of Business Organization as of September 30, 1990

Dollars in millions

Organization type	Outstanding principal	Default percentage	Liquidation percentage	Nonperformance percentage
Corporation	$6,057.1	5.6	11.2	16.8
Partnership	1,186.1	5.0	8.5	13.5
Individual	3,067.8	5.7	7.3	13.0
Missing value	0.3			
Total[a]	**$10,311.2**			

[a]Total may not add because of rounding.

Substantial Variance in Loan Performance Exists by Race of Borrower

Within the 7(a) portfolio, the percentage of nonperforming loans varies substantially by race. As shown in table III.8, black borrowers have the highest percentage of nonperforming loans at about 36 percent. Loans received by Puerto Rican borrowers show the next highest percentage of nonperformance at 30 percent. White borrowers, who have the largest number and dollar volume of outstanding loans, have a nonperformance

rate of about 14 percent. Asian borrowers have the best loan performance; about 12 percent of their loans are either in liquidation or in default.

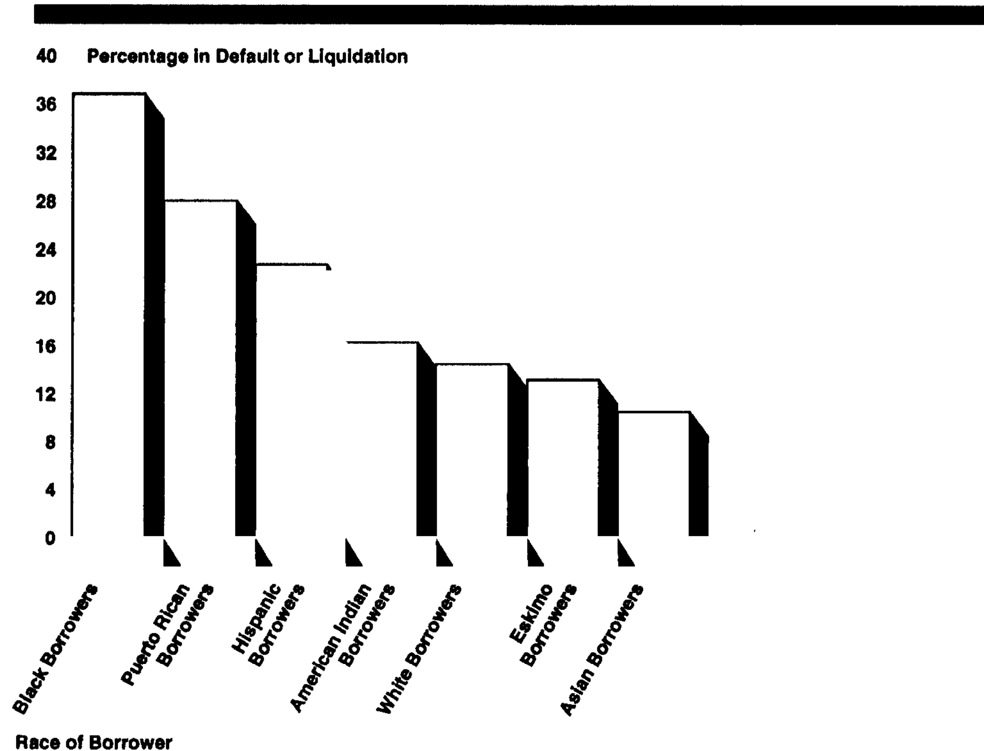
Table III.8: Performance of 7(a) Portfolio by Race of Borrower as of September 30, 1990

Dollars in millions

Race	Outstanding principal	Default percentage	Liquidation percentage	Number of loans	Default percentage	Liquidation percentage
Black	$317.9	10.6	26.2	4,406	13.2	22.9
Puerto Rican	147.9	11.0	17.0	2,372	10.4	19.4
Hispanic	312.9	8.3	14.4	3,478	10.8	14.3
Amer. Indian	41.8	6.2	10.1	439	6.4	11.6
White	8,797.6	5.2	9.2	74,402	5.9	8.6
Eskimo	3.2	6.8	6.4	30	16.7	10.0
Other	23.4	5.5	6.5	129	7.0	9.3
Asian	514.5	5.1	5.3	3,496	5.7	6.1
Undetermined	152.2	3.3	4.8	1,015	3.9	5.8
Total[a]	**$10,311.2**			**89,767**		

[a]Total may not add because of rounding.

Figure III.4: Percentage of Outstanding Principal in Default or Liquidation by Race of Borrower as of September 30, 1990



Nonperformance Rates for Male and Female Borrowers Are Similar

Performance statistics for male and female borrowers are similar; one point separates their liquidation percentages and even less distinguishes their respective default percentages. Of the $9.3 billion lent to male borrowers, about $890 million, or 9.6 percent, was in liquidation as of September 30, 1990. Similarly, $104 million, or 10.6 percent, of the $978-million outstanding principal lent to females was in liquidation.

Table III.9: Performance of 7(a) Portfolio by Borrower Gender as of September 30, 1990

Dollars in millions

Gender	Outstanding principal	Default percentage	Liquidation percentage	Number of loans	Default percentage	Liquidation percentage
Women	$978.5	6.1	10.6	11,160	7.8	10.1
Men	9,313.0	5.5	9.6	78,039	6.4	9.5
Missing value	19.8			568		
Total[a]	**$10,311.2**			**89,767**		

[a]Total may not add because of rounding.

Figure III.5: Performance of Loans Made to Female Borrowers as a Percentage of Outstanding Principal as of September 30, 1990

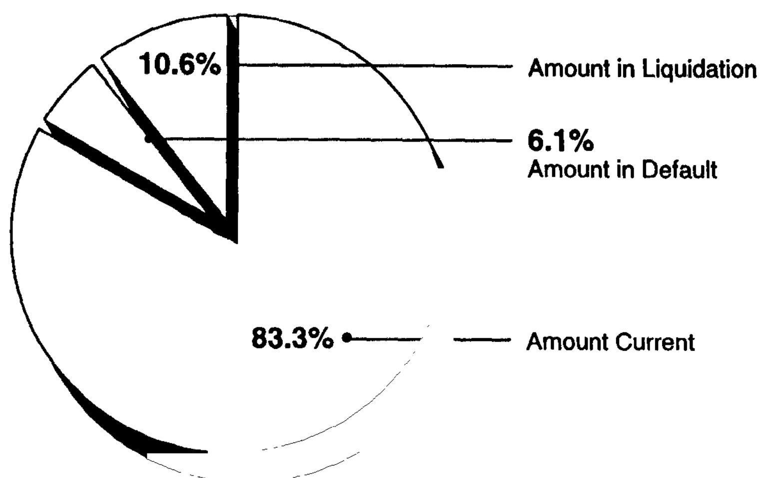
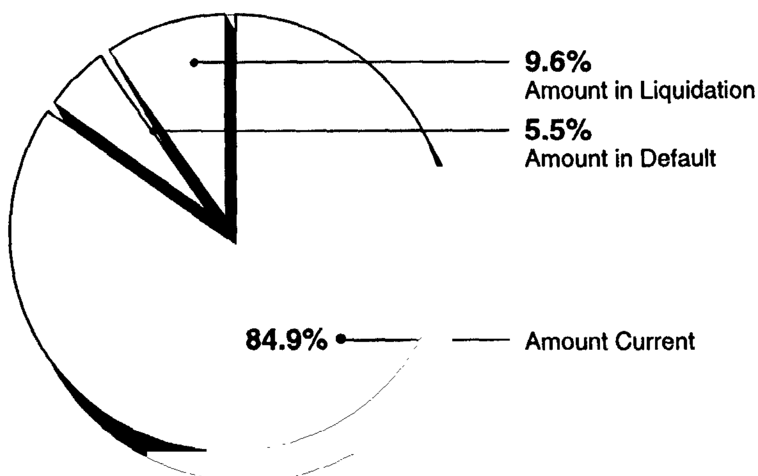


Figure III.6: Performance of Loans Made to Male Borrowers as a Percentage of Outstanding Principal as of September 30, 1990



7(a) Loan Performance Varies by State

Among states, default and liquidation percentages vary substantially. The highest nonperformance percentage, 38.9 percent, is found in the District of Columbia. Small businesses in California, which had over $1.8 billion in outstanding principal as of September 30, 1990—more SBA 7(a) money than any other state—had a relatively low nonperformance percentage, 8.9 percent. That percentage, however, represents over $160 million in outstanding principal. Table III.10 shows the 10 states with the highest nonperformance percentages and the 10 states with the

lowest nonperformance percentages. Table III.11 contains details on 7(a) loan performance in all states.

Table III.10: States With the Highest and Lowest Nonperformance Percentages as of September 30, 1990

Dollars in millions

State	Outstanding principal	Default percentage	Liquidation percentage	Nonperformance percentage
Highest nonperformance percentages:				
District of Columbia	$9.9	10.4	28.5	38.9
Alaska	197.2	17.0	18.2	35.2
Rhode Island	37.7	14.9	15.1	30.1
Connecticut	56.8	10.2	16.9	27.2
Louisiana	100.8	10.7	15.8	26.5
Illinois	354.2	5.2	21.2	26.4
Delaware	8.0	11.6	13.8	25.4
Indiana	111.9	6.7	16.0	22.7
Arizona	131.5	6.2	16.2	22.4
Oklahoma	138.4	5.4	17.0	22.3
Total[a]	**$1,146.4**			
Total Percentage		8.6	18.2	26.8
State	**Outstanding principal**	**Default percentage**	**Liquidation percentage**	**Nonperformance percentage**
Lowest nonperformance percentages:				
Oregon	$90.5	1.5	5.0	6.4
Idaho	98.5	2.9	3.6	6.4
Montana	248.4	2.3	5.0	7.2
South Dakota	117.3	1.6	5.7	7.2
Alabama	136.2	3.2	5.5	8.7
California	1,801.4	3.4	5.5	8.9
Iowa	229.7	3.8	5.3	9.1
Tennessee	208.7	1.8	7.4	9.2
Wisconsin	394.6	4.4	4.9	9.4
North Carolina	97.9	2.7	7.4	10.1
Total[a]	**$3,423.1**			
Total Percentage		3.2	5.5	8.7

[a]Total may not add because of rounding.

Table III.11: Performance of 7(a) Portfolio by State and Territory as of September 30, 1990

	Amount current or deferred	Amount in default	Amount in liquidation	Total outstanding principal	Default percentage	Liquidation percentage	Nonperformance percentage
Alabama(47)	$124,425,251	$4,348,008	$7,464,203	$136,237,462	3.2	5.5	8.7
Alaska(2)	127,814,625	33,499,706	35,887,952	197,202,283	17.0	18.2	35.2
Arizona(9)	102,059,054	8,143,706	21,268,373	131,471,133	6.2	16.2	22.4
Arkansas(33)	49,808,726	2,678,007	5,277,134	57,763,867	4.6	9.1	13.8
California(46)	1,641,043,401	60,772,825	99,601,917	1,801,418,143	3.4	5.5	8.9
Colorado(27)	154,762,487	9,643,221	18,484,009	182,889,717	5.3	10.1	15.4
Connecticut(4)	41,397,177	5,809,134	9,619,767	56,826,078	10.2	16.9	27.2
Delaware(7)	5,982,676	931,527	1,108,026	8,022,229	11.6	13.8	25.4
Dist. of Col.(1)	6,074,733	1,033,806	2,832,390	9,940,929	10.4	28.5	38.9
Florida(11)	182,928,203	15,378,230	33,567,576	231,874,009	6.6	14.5	21.1
Georgia(34)	445,117,100	27,956,901	39,596,776	512,670,777	5.5	7.7	13.2
Hawaii(28)	22,136,224	2,275,002	1,721,611	26,132,837	8.7	6.6	15.3
Idaho(50)	92,208,662	2,816,394	3,521,462	98,546,525	2.9	3.6	6.4
Illinois(6)	260,784,344	18,364,068	75,048,934	354,197,346	5.2	21.2	26.4
Indiana(8)	86,491,671	7,490,491	17,873,340	111,855,502	6.7	16.0	22.7
Iowa(45)	208,724,064	8,769,186	12,174,059	229,667,309	3.8	5.3	9.1
Kansas(24)	200,825,038	10,463,256	29,749,459	241,037,753	4.3	12.3	16.7
Kentucky(22)	136,119,794	11,927,774	16,272,399	164,319,967	7.3	9.9	17.2
Louisiana(5)	74,073,155	10,761,018	15,932,213	100,766,386	10.7	15.8	26.5
Maine(39)	73,179,197	5,507,168	3,359,314	82,045,679	6.7	4.1	10.8
Maryland(15)	45,223,673	3,975,672	6,813,970	56,013,315	7.1	12.2	19.3
Massachusetts(19)	93,974,448	3,383,752	17,927,707	115,285,907	2.9	15.6	18.5
Michigan(18)	143,072,401	9,664,135	22,850,986	175,587,522	5.5	13.0	18.5
Minnesota(41)	168,901,520	8,884,241	10,869,649	188,655,410	4.7	5.8	10.5
Mississippi(21)	58,260,041	3,224,136	9,063,046	70,547,223	4.6	12.8	17.4
Missouri(30)	239,807,758	20,466,075	20,285,133	280,558,966	7.3	7.2	14.5
Montana(49)	230,458,973	5,597,802	12,324,679	248,381,454	2.3	5.0	7.2
Nebraska(37)	84,672,463	5,277,075	5,870,936	95,820,474	5.5	6.1	11.6
Nevada(40)	40,938,210	3,275,870	1,635,925	45,850,005	7.1	3.6	10.7
New Hampshire(25)	71,904,741	7,109,967	6,918,012	85,932,720	8.3	8.1	16.3

(continued)

	Amount current or deferred	Amount in default	Amount in liquidation	Total outstanding principal	Default percentage	Liquidation percentage	Nonperformance percentage
New Jersey(17)	129,711,840	11,187,825	18,307,296	159,206,961	7.0	11.5	18.5
New Mexico(31)	106,251,623	7,554,827	9,980,573	123,787,023	6.1	8.1	14.2
New York(13)	422,273,206	34,174,068	69,470,124	525,917,398	6.5	13.2	19.7
North Carolina(42)	88,030,353	2,635,303	7,260,167	97,925,823	2.7	7.4	10.1
North Dakota(16)	58,922,557	6,399,226	7,137,911	72,459,694	8.8	9.9	18.7
Ohio(12)	196,459,646	16,056,289	35,787,074	248,303,009	6.5	14.4	20.9
Oklahoma(10)	107,448,059	7,409,928	23,513,902	138,371,889	5.4	17.0	22.3
Oregon(51)	84,637,507	1,311,942	4,504,708	90,454,157	1.5	5.0	6.4
Pennsylvania(20)	164,978,749	11,134,217	25,844,541	201,957,507	5.5	12.8	18.3
Rhode Island(3)	26,395,188	5,637,555	5,702,997	37,735,740	14.9	15.1	30.1
South Carolina(29)	71,916,130	2,909,713	9,499,177	84,325,020	3.5	11.3	14.7
South Dakota(48)	108,785,616	1,835,964	6,650,622	117,272,202	1.6	5.7	7.2
Tennessee(44)	189,497,068	3,722,632	15,447,852	208,667,552	1.8	7.4	9.2
Texas(14)	652,246,224	64,274,366	92,969,070	809,489,660	7.9	11.5	19.4
Utah(26)	128,463,999	9,906,810	13,752,524	152,123,333	6.5	9.0	15.6
Vermont(38)	163,696,461	15,238,506	4,757,702	183,692,669	8.3	2.6	10.9
Virginia(32)	52,419,882	2,823,741	5,772,386	61,016,009	4.6	9.5	14.1
Washington(36)	203,825,495	7,172,060	20,669,950	231,667,505	3.1	8.9	12.0
West Virginia(23)	40,694,701	1,937,944	6,316,802	48,949,447	4.0	12.9	16.9
Wisconsin(43)	357,544,616	17,544,685	19,483,168	394,572,469	4.4	4.9	9.4
Wyoming(35)	75,830,599	5,233,798	5,649,159	86,713,556	6.0	6.5	12.6
Territories[a]	93,471,939	16,552,752	28,152,478	138,177,169	12.0	20.4	32.4
Missing value	782,440	22,929	138,412	943,781	5.5	9.7	15.3
Total	**$8,737,453,715**	**$572,105,233**	**$1,001,689,552**	**$10,311,248,500**			

Note: The number in parentheses ranks each state according to the percentage of outstanding principal either in default or in liquidation. For example, the District of Columbia, which has the highest percentage of nonperforming loans ranks first.

[a]Include American Samoa, Guam, Puerto Rico, and Virgin Islands.

Loan Losses in the 7(a) Portfolio

Loss Rate Is Greater for Direct Loans Than for Guaranteed Loans

Of the $5.3 billion disbursed in direct loans between 1954 and 1989, about $870 million has been charged off as a loss (for an overall loss rate of 16.4 percent). For the same period, the overall loss rate for guaranteed loans stood at 9.4 percent. After a first-year loss rate that was 18 percent of the total loan amount disbursed by SBA, the direct loan program settled down to a loss rate of about 4 percent during the 1950s. Losses increased slightly in the 1960s to around 6 percent of the amount disbursed but rose sharply in the 1970s and early 1980s, climbing to over 32 percent in 1977 and 1979. According to SBA, these escalating losses were due to increased lending and a lenient application of the direct loan program's credit standards. SBA officials stated that, in recent years, SBA has evaluated credit risk more carefully, as evidenced by the improved loss rates since 1984. According to the officials, however, the overall loss rate for the direct loan program remains high because SBA lent out a large portion of the direct loan portfolio before it revised its policy for evaluating credit qualifications.

For guaranteed loans, loss rates have remained relatively constant. Although loss rates were especially low (around 1 percent) during the first 10 years of the program when most of SBA's lending was made through direct loans, they generally remained between 8 and 15 percent throughout the late 1960s, the 1970s, and the early 1980s.

Although loss rates for both the direct and guaranteed programs have been low during the last few years, these low loss rates are not completely related to improved loan performance. On average, SBA loans that result in losses do not go into liquidation until 3 years after loan approval. As a result, loans approved since 1987 have not been active long enough for their true performance to be measured. Table IV.1 provides information on direct loan losses and table IV.2 provides information on guaranteed loan losses over the life of the 7(a) programs.

Table IV.1: Direct Loan Losses as of September 30, 1990

Dollars in thousands

Fiscal year	Amount disbursed	Amount charged off	Loss rate	Outstanding principal	
				In liquidation	Not in liquidation
1954	$1,967.8	$354.3	18.0	$0	$0
1955	18,826.4	605.4	3.2	0	0
1956	28,806.8	1,333.7	4.6	0	0
1957	79,330.2	2,787.4	3.5	0	0
1958	109,638.4	3,434.3	3.1	0	0
1959	164,260.9	6,968.5	4.2	0	0
1960	125,158.8	3,363.7	2.7	0	0
1961	147,316.8	5,288.3	3.6	0	0
1962	258,186.7	8,227.4	3.2	0	0
1963	194,083.0	6,491.6	3.3	19.5	0
1964	188,451.6	10,320.6	5.5	0	0
1965	283,113.7	20,500.0	7.2	0	148.0
1966	205,364.5	19,233.2	9.4	42.3	6.6
1967	172,405.2	19,322.8	11.2	99.7	4.9
1968	222,479.7	17,706.5	8.0	42.4	114.9
1969	143,935.1	14,873.3	10.3	0	67.1
1970	119,334.5	19,360.3	16.2	181.6	144.9
1971	119,696.5	28,559.6	23.9	252.1	418.6
1972	129,912.3	31,578.7	24.3	267.8	413.2
1973	125,512.3	35,766.8	28.5	630.4	659.0
1974	99,761.8	30,003.2	30.1	1,065.7	1,078.7
1975	132,405.6	36,406.7	27.5	1,053.8	2,261.2
1976	195,643.3	40,356.8	20.6	1,122.3	3,269.8
TQ[a]	46,501.1	9,784.4	21.0	653.8	1,320.7
1977	198,038.4	66,093.7	33.4	4,001.6	12,801.3
1978	259,592.3	69,221.0	26.7	4,844.1	20,289.4
1979	246,394.0	79,739.1	32.4	8,173.2	28,594.4
1980	314,440.5	90,069.1	28.6	8,926.8	30,813.7
1981	244,724.2	68,564.1	28.0	9,615.6	34,244.4
1982	169,717.6	33,813.7	19.9	4,826.5	16,682.8
1983	109,199.5	25,234.4	23.1	6,341.9	24,942.0
1984	139,270.2	31,239.0	22.4	10,914.4	27,069.2
1985	123,549.8	20,547.5	16.6	9,038.2	33,738.7
1986	62,278.4	5,435.2	8.7	2,976.9	19,615.3
1987	42,938.0	4,146.1	9.7	5,049.3	21,799.5
1988	39,777.2	3,209.6	8.1	4,167.1	26,422.0

(continued)

Fiscal year	Amount disbursed	Amount charged off	Loss rate	Outstanding principal	
				In liquidation	Not in liquidation
1989	45,597.7	547.5	1.2	2,883.5	35,135.7
Total[b]	**$5,307,610.8**	**$870,487.4**		**$87,190.5**	**$342,056.0**
Overall rate			16.4		

[a]TQ represents the activity that took place during the "transitional quarter" that occurred when the federal government changed the last month of the fiscal year from June to September.

[b]Total does not account for the $39.6 million in direct loans disbursed in 1990 because, as of September 30, 1990, only one of these loans had been charged off, for a loss of about $39,000.

Table IV.2: Guaranteed Loan Losses as of September 30, 1990

Dollars in thousands

				Outstanding principal	
Fiscal year	Amount disbursed	Amount charged off	Loss rate	In liquidation	Not in liquidation
1954	$2,253.5	$110.2	4.9	$0	$0
1955	16,355.1	146.0	0.9	0	0
1956	14,661.9	229.9	1.6	0	0
1957	16,559.0	127.3	0.8	0	0
1958	15,196.2	226.5	1.5	0	0
1959	22,726.7	407.7	1.8	0	0
1960	21,137.3	106.0	0.5	0	0
1961	11,683.7	75.3	0.6	0	0
1962	20,722.6	124.1	0.6	0	0
1963	20,388.0	93.9	0.5	0	0
1964	14,563.1	353.2	2.4	0	0
1965	35,016.2	2,668.3	7.6	0	44.9
1966	67,795.0	5,556.9	8.2	0	14.7
1967	102,464.6	4,522.3	4.4	0	0
1968	129,647.1	10,557.9	8.1	12.4	49.7
1969	230,829.0	31,482.8	13.6	62.6	293.3
1970	296,329.0	41,420.1	14.0	188.2	348.6
1971	331,326.6	67,335.6	20.3	1,351.4	1,271.8
1972	1,104,537.5	95,704.6	8.7	1,680.5	910.7
1973	1,311,548.8	175,048.0	13.3	1,939.8	5,379.1
1974	1,339,590.4	160,023.8	11.9	3,177.7	5,711.2
1975	1,048,010.1	95,814.4	9.1	1,630.3	2,839.6
1976	1,332,876.0	123,393.8	9.3	5,379.8	9,761.7
TQ[a]	376,943.4	35,165.0	9.3	1,977.7	6,404.7
1977	1,774,753.9	187,744.7	10.6	15,068.4	64,936.3
1978	1,923,072.8	237,695.0	12.4	24,407.9	108,638.8
1979	2,269,855.9	301,537.7	13.3	39,015.4	128,951.0
1980	2,415,510.6	459,271.5	19.0	55,280.1	109,736.4
1981	2,486,094.5	420,911.7	16.9	55,694.2	117,017.8
1982	2,117,494.0	154,168.9	7.3	31,198.9	103,147.3
1983	1,578,478.2	177,604.9	11.3	61,524.0	271,643.2
1984	2,130,670.5	206,775.8	9.7	91,802.0	429,486.5
1985	2,099,949.2	141,116.2	6.7	99,249.3	579,132.5
1986	1,458,015.6	78,447.0	5.4	105,092.3	778,476.3
1987	2,372,234.4	47,824.1	2.0	121,142.8	1,129,906.1
1988	2,043,543.1	23,103.6	1.1	123,599.4	1,511,841.0

(continued)

Fiscal year	Amount disbursed	Amount charged off	Loss rate	Outstanding principal: In liquidation	Outstanding principal: Not in liquidation
1989	2,393,520.2	6,513.2	0.3	69,271.6	2,025,647.8
Total[b]	**$34,946,353.9**	**$3,293,408.6**		**$909,746.6**	**$7,391,590.9**
Overall rate			9.4		

[a]TQ represents the activity that took place during the "transitional quarter" that occurred when the federal government changed the last month of the fiscal year from June to September.

[b]Totals do not account for the $2.6 billion disbursed in 1990 because, as of September 30, 1990, only four loans had been charged off, for a loss of about $68,000.

SBA officials noted that our method of calculating loan losses differs substantially from that used by banks, and, therefore, our loss figures for SBA loans should not be compared to bank loss figures for their loans. The officials stated that although our methodology provides useful information about SBA policies in effect at the time the loans were made, the difference between the two methods of calculating losses should be explained.

We calculated losses by determining the percentage of funds disbursed in a particular fiscal year that were eventually charged off as a loss. For example, table IV.1 shows that in fiscal year 1980, SBA disbursed about $314 million in direct loans, of which about $90 million, or 28.6 percent, was eventually charged off as a loss. (The year the loan was charged off is not shown because, according to SBA, the actual charge-off is an administrative action that indicates very little about when the loan encountered performance problems.)

Banks, however, calculate losses for the year by determining the percentage of average outstanding principal that was charged off as a loss during the year. According to SBA officials, when SBA loan losses are calculated using the banks' method, the loss figures are lower. As shown in table IV.3, SBA provided a comparison of loss rates, calculated according to the banks' method, for the SBA 7(a) guaranteed portfolio and for commercial and industrial loans made by banks insured by the Federal Deposit Insurance Corporation (FDIC).

Table IV.3: SBA's Comparison of Loan Loss Rates for SBA Loans and Bank Business Loans

Loss rates in percent

	Loss rates	
Year	SBA	Bank[a]
1984	2.9	1.3
1985	2.0	1.4
1986	3.5	1.5
1987	3.8	1.2
1988	3.7	1.1

[a]SBA used FDIC's Statistics on Banking to calculate the bank loss rates. SBA officials believe that losses for 7(a) loans and bank business loans are only comparable since 1984 because, before that time, the FDIC business loan data did not show commercial and industrial loans separately but combined them with real estate, credit card, and installment loans.

Note: The data are shown by fiscal year for SBA loans, as maintained in SBA's data base, and by calendar year for bank loans, as presented in Statistics on Banking. The most recent figures published in Statistics on Banking are for 1988.

Source: SBA.

Guaranteed Loans Made by Regular Lenders Have the Highest 7(a) Loss Rates

Overall, loss rates for regular loans are significantly higher (8.5 percent) than loss rates for both certified and preferred loans (2.5 percent and 0.3 percent, respectively). These data are correlated with the performance data presented in appendix III of this report, which show that regular loans also have a higher default and liquidation rate than loans made under the other two lender programs. This disparity can be explained by the higher credit standards applied to certified and preferred lender loans. For example, SBA's lending guidelines state that preferred lender loans should be made to more creditworthy borrowers because SBA does not approve these loans and the guarantee percentage for the lender is reduced. However, as stated previously, a true loss rate cannot be calculated for recently made loans because sufficient time has not passed to judge their performance. As a result, the overall performance of preferred lender loans, which were not made until 1983 and currently have an especially low loss rate, cannot yet be determined.

Because SBA does not keep data on actual disbursements by type of lender program, our calculations of lender program loss rates are based on the amounts approved for lending rather than on the amounts disbursed. SBA estimates that about 15 percent of the funds approved for lending are not disbursed because of loan cancellations and other individual borrower circumstances.

Table IV.4: Loss Rates by Type of Lender Program as of September 30, 1990

Dollars in millions

Type of lender	Total amount approved	Total amount charged off	Loss rate
Regular (1954)[a]	$37,031.2	$3,158.0	8.5
Certified (1979)[a]	5,197.1	130.5	2.5
Preferred (1983)[a]	1,681.9	5.4	0.3
Total amount[b]	**$43,910.2**	**$3,293.9**	

[a]The numbers in parentheses indicate the year in which the lender programs began.

[b]Totals may not add because of rounding.

Special Loan Programs Have a Higher Loss Rate Than the General Business Loan Program

Losses incurred by the general business loan program produce a loss rate that, at 9 percent, is significantly lower than that of SBA's special loan programs. Of the special programs, handicapped assistance loans show the lowest loss rate at almost 12 percent, but energy loans have a rate of loss of almost 41 percent. As stated previously, SBA officials explained the poor performance of some of the special programs by stating that most of the principal outstanding in these programs was lent at a time when SBA was leniently applying credit standards to benefit as many people as possible. The officials stated that in recent years, however, SBA has more carefully evaluated credit risk, since loans that perform poorly ultimately benefit neither SBA nor the borrower. It should be noted, however, that these programs have received significantly less funding than the general business programs. Since program inception, SBA has disbursed about $41 billion for general business loans, compared with about $2 billion for special loans.

Table IV.5: Loss Rates by Loan Program as of September 30, 1990

Dollars in millions

Program	Total amount disbursed	Total amount charged off	Total loss rate
General business (1954)[a]	$41,043.3	$3,689.4	9.0
Economic opportunity (1965)[a]	1,488.0	408.6	27.5
Handicapped assistance (1974)[a]	242.1	28.3	11.7
Energy (1979)[a]	53.9	22.0	40.8
Veterans (1983)[a]	100.5	16.3	16.2
Minority business (1989)[a]	2.3	0[b]	
Total amount[c]	**$42,930.2**	**$4,164.6**	
Overall rate			9.7

[a]The numbers in parentheses indicate the first year in which any funds were disbursed for each program.

[b]Fiscal year 1989 was the first year in which any loans were disbursed. Consequently, no loans have yet been charged off.

[c]Totals may not add because of rounding.

Objectives, Scope, and Methodology

In September 1990, the Chairman of the House Committee on Small Business requested that we analyze SBA's 7(a) business loan portfolio, the largest of SBA's financial assistance programs. In subsequent discussions with the Chairman's office, we agreed to provide (1) an overview of the portfolio as of September 30, 1990, including information on total debt and total number of direct and guaranteed loans in the portfolio, by loan program and by type of lender program, and some demographic data on borrowers, including their race, gender, geographic location, business type, and organization type; (2) information on the performance of the portfolio as shown by the amount of outstanding principal that was current, in default, or in liquidation; and (3) statistics on overall losses by year in the direct and guaranteed 7(a) portfolio and on losses incurred by loan program and type of lender. Generally, the information in this report about the 7(a) loan portfolio is based on data available as of September 30, 1990. However, because banks report to SBA on a quarterly basis, the data tape information on guaranteed loans shows actual loan activity as of July 30, 1990.

The scope of our analysis included the major financial assistance programs established by section 7(a) of the Small Business Act and its various subsections. These are also the loan programs that are included in SBA's Management Information Summary (MIS) in the business loan portfolio section. This MIS report is issued monthly by the Office of Financial Management and is an agencywide status report of SBA's financial assistance programs. The MIS report also includes in its business section information on investment and development companies. As agreed with the Chairman's office, we did not include data on these programs because both programs began as part of a different piece of legislation, the Small Business Investment Act. Our analysis is limited to the general business program and the most significant special loan programs that are authorized by subsections of section 7(a), including the economic opportunity, handicapped assistance, veterans, energy, and minority business programs.

We obtained the information used in this report from three main sources. First, data for appendixes II and III on active loans as of September 30, 1990, and data for appendix IV on loan losses came from data tapes provided by SBA from its automated loan accounting system data base, which is maintained by the agency's Office of Financial Management. Second, the fiscal year 1981 to 1990 trend information on outstanding principal and loans came from each year's September Management Information Summary. Finally, in order to calculate loss

rates in appendix IV, we obtained data on loan approvals and disbursements by year and disbursements by program from SBA's Office of Accounting Operations. By lender, SBA keeps data on funds approved for lending only, not disbursements, and so we calculated lender loss rates on the basis of funds approved. Because SBA does not keep data on funds disbursed or approved by race, gender, or the other demographic characteristics used in appendixes II and III of this report, we could not calculate loss rates by these characteristics. Unless noted otherwise, the source for our tables is our analysis of SBA's data tapes. When we used any other sources for specific tables, we stated the other source.

SBA's data base includes information on three types of loans: direct, immediate participation, and guaranteed. Because direct and immediate participation loans both involve an initial outlay of funds by SBA, we combined these two types of loans in our analysis, as SBA does for its management information reports. In addition, SBA differentiates between outstanding loan guarantees and loan guarantees that SBA has had to purchase. SBA makes this distinction to show loan performance. Our study determined loan performance by the amount of total outstanding principal that was current, in default, or in liquidation. As a result, we omitted the distinction between outstanding guarantees and purchased guarantees except where this distinction seemed essential.

As described in appendix I, SBA uses five different categories to define loan status: current, deferred, past due, delinquent, and in liquidation. To simplify our presentation, we placed loans into only three categories. We combined current and deferred loans into one "current" category because deferred loans have had their due date extended and are not considered overdue. We also combined past due loans (those that are one payment overdue) and delinquent loans (those that are more than one payment overdue) into one category and classified them as loans "in default." We did this because these loans have the common feature of having missed at least one loan payment but are not yet in liquidation. We kept SBA's classification of loans in liquidation.

Reliability Assessment

Because our analysis relied primarily on SBA's loan accounting system data base, we used two methods to ensure the reliability of the data. First, we discussed policy and procedures for maintaining the data base with SBA's headquarters and district office personnel to determine the procedural risk in the system. Second, we performed a two-part reliability assessment in which we conducted tests to determine whether the proper data had been accurately and completely transferred from hard

copy into the data base. For the accuracy test, we drew a sample of records from the data base in three high-volume SBA offices and compared these records with the original documents in the loan files. For the completeness test, we compared the numbers and dollar amounts of loans from the tapes that we received from SBA for the 7(a) portfolio as of September 30, 1990, with the same aggregate information published by SBA in its MIS report.

Evaluation of Procedures

On the basis of both our discussions with agency officials on policy and procedures for maintaining the data base and our observation of these procedures in use, we determined that the procedural reliability risk is low because of internal management controls and inherent controls on the system stemming from the different parties involved in each loan. An example of an internal control is the SBA policy that, for an action to be taken on a loan file, two people—a recommending official and an approving official—must agree that the action is appropriate and necessary before it can be entered into the system. An example of a systemic control is that, in the case of guaranteed loans, the borrower, the lender, and SBA all have individual and different reasons for ensuring that many of the data fields used in our analysis—such as the interest rate and amount outstanding—are correct. Direct loans have just two parties, the borrower and SBA, to ensure the accuracy of the data elements. The divergent interests of these parties serve as external checks on the data base.

Accuracy Test

As of September 30, 1990, SBA's loan accounting system data base contained 89,767 records. We visited three offices, two high loan volume district offices—one in Chicago and one in Atlanta—and the servicing center in Fresno, California, which services all current business loans made in the states of California, Nevada, and Arizona. At each of these locations we selected a separate simple random sample of loan files. Table V.1 shows the universe and sample size for each location.

Table V.1: Loan Universe and Sample Size of Locations Reviewed

Location	Universe size	Sample size
Atlanta	2,807	68
Chicago	1,776	73
Fresno	10,014	69
Total	**14,597**	**210**

For each loan record selected, we verified the accuracy and reliability of 23 data fields, comparing the data in the data base to the data found in the original loan file at the field office. Table V.2 summarizes the results of this analysis. It gives the estimate for the office that had the highest number of errors in our sample for the specified data element.

Since we used a sample (called a probability sample) of loan files, each estimate developed from the sample has a measurable precision. The precision indicates how closely we can reproduce from a sample the results that we would obtain if we were to take a complete count of the universe using the same measurement methods. To indicate the precision of each of our estimates, we provide a range called a confidence interval that was developed at the 95- percent level of confidence. This confidence interval at the 95-percent confidence level indicates that in 95 out of 100 instances, the sampling procedure we used would produce a confidence interval containing the universe value we are estimating.

Table V.2: Accuracy Test Results for the Three Offices Reviewed (Estimate for the Office With the Highest Observed Error Rate)

SBA data base field name	Number of errors	Estimated percentage of records in error	Lower bound of error (percent)	Upper bound of error (percent)
Loan number	0	[a]	0.0	5.4
State	1	1.4	0.1	7.2
Office	0	[a]	0.0	5.4
Original loan type	0	[a]	0.0	5.4
Current loan type	1	1.4	0.1	7.2
Organization code	4	5.9	1.8	13.9
Bank code	2	2.9	0.4	9.9
Major program code	0	[a]	0.0	5.4
SIC code	3	4.4	1.0	11.9
Minority code	6	8.7	3.5	17.4
Gender code	5	7.4	2.7	15.8
SBA percentage	2	2.9	0.4	10.0
SBA interest	0	[a]	0.0	5.4
Bank interest (b)	8	11.8	3.3	20.3
Maturity months (c)	14	19.2	9.4	28.9
Loan status	1	1.5	0.1	7.8
Total amount outstanding	1	1.5	0.1	7.8
SBA amount outstanding	3	4.4	1.0	12.0
Bank number	0	[a]	0.0	5.4
Bank name	0	[a]	0.0	5.4
Social Security number	1	1.5	0.1	7.8
IRS number	0	[a]	0.0	5.4
Loan approval date	0	[a]	0.0	5.4

[a]Since we observed no errors, we provide only the lower and upper bounds for the estimate, using the calculation approximated from the Poisson distribution.

[b]The errors generally occurred with variable-rate loans because of a lag in data entry that occurs as a result of the constant interest rate fluctuation associated with these types of loans.

[c]Nine of the 14 errors occurred in liquidated loans. In some instances, the maturity months had been changed to reflect the remaining months outstanding on the loan instead of the term of the loan when the loan was approved. SBA officials stated that these changes would reflect the effect of deferments granted during the life of the loan.

Completeness Test

To test for the completeness of the data base, we compared the numbers and dollar amounts of loans from the data tape we received from SBA for the 7(a) portfolio as of September 30, 1990, to the relevant information published by SBA in its Management Information Summary report.

As of September 30, 1990, excluding development companies, the data tape we received from SBA contained 89,767 records valued at $10,311.2 million, as compared with 106,218 records valued at $12,698.1 million on the September 30, 1990 MIS report. After we subtracted development company loans from the MIS numbers for consistency, we brought the MIS totals down to 95,494 records valued at $10,677.3 million. The adjusted MIS numbers showed 5,727 records and $366.1 million more than our data tape.

We asked SBA officials to account for this difference. They explained that the MIS report contains not only loans but also three types of liquidation asset accounts. These are accounts that are set up for loans that SBA liquidates. The original loan account is closed and therefore would not appear on our data tape. However, these liquidation asset accounts are included in the MIS report but not specifically identified. Because our report includes only loans and not these other accounts, the MIS report lists a larger number of accounts. We obtained the number and dollar value of these accounts from SBA officials as of September 30, 1990.

The following types of accounts make up the MIS liquidation asset accounts as of September 30, 1990:

- 5,560 note receivable accounts valued at $402.1 million. A note receivable account may be established when a note receivable has been used to satisfy the debt on the original loan. For example, this arrangement may occur when a guarantor or a partner in the business assumes the indebtedness as personal debt.
- 361 collateral purchased accounts valued at $117 million. SBA sets up these accounts when a loan is liquidated and the borrower's collateral is purchased. The account includes the costs incurred by SBA during liquidation for acquiring land, buildings, and other property.
- 202 judgment accounts valued at $56 million. When a loan goes into liquidation and SBA is unable to collect on the loan, SBA may go to court to seek a legal judgment to satisfy the debt. In these cases, a separate judgment account may be established.

When these liquidation asset accounts are subtracted from the MIS data, the adjusted MIS numbers are 89,371 records valued at $10,102.1 million. These totals are 396 records fewer and $209.1 million less than the totals on our data tape. The dollar discrepancy is 2 percent of the total dollar amount of the loans on our tape ($10.3 billion), and the difference in numbers of loans is 0.4 percent of the total number of records on our data tape (89,767). SBA officials could not explain this final discrepancy

in numbers but believed that the difference was too small to affect the accuracy of our analysis.

Data Conclusions

Our data reliability assessment was limited to (1) verifying the procedural reliability of the data base, (2) ensuring the accuracy of selected data base fields, and (3) determining the completeness of the data we received on SBA's data tapes. Since we are not using SBA's automated data as a basis for conclusions, we found that SBA's loan accounting system data base was acceptable for performing our analysis.

Our work was performed between October 1990 and June 1991 in accordance with generally accepted government auditing standards. We discussed the report's contents with officials from SBA's Financial Assistance Division and have incorporated their comments where appropriate. These officials generally agreed that the report accurately represents the composition and performance of the 7(a) portfolio. However, as agreed with your office, we did not obtain written agency comments.

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