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### MICROLOAN PROGRAM IMPROVEMENT ACT OF 2001

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Mr. BOND, from the Committee on Small Business,  
submitted the following

### REPORT

[To accompany S. 174]

On February 28, 2001, the Senate Committee on Small Business considered the bill (S. 174) to amend the Small Business Act with respect to the Microloan Program, and for other purposes. The bill amends the Small Business Administration's Microloan Program to make it more flexible to meet credit needs, more accessible to micro-entrepreneurs across the nation, and more streamlined for lenders to make loans and provide management assistance, and for other purposes. Having considered S. 174, the Committee reports favorably thereon without further amendment and recommends that the bill do pass.

#### I. DESCRIPTION OF BILL

This legislation complements programmatic and technical changes made during the last Congress to the Small Business Administration's Microloan Program. The Committee is very supportive of this program and worked with industry and the SBA to develop these changes.

Congress created the Microloan Program as a pilot in 1991 (Public Law 102-140) to reach very small businesses that were not being served by traditional lenders of SBA's credit programs. These microentrepreneurs, who are often minorities, women, and low-income individuals, needed very little money to launch a business. They could not get loans because they were considered unreliable or risky borrowers by traditional credit markets. Their weak or non-existent credit histories or limited business experience caused traditional commercial lenders to shy away from making such

loans. To fill this credit need, the Microloan Program was designed to provide loans to non-profit intermediary lenders, who in turn provide fixed-rate loans of not more than \$25,000, and on average, loans less than \$10,000, to very small businesses. Last year, Congress approved legislation increasing the maximum loan limit from \$25,000 to \$35,000 (Section 210(a)(1) of P.L. 106-554); the average loan size limit was increased from not more than \$10,000 to not more than \$15,000 (Section (a)(5) of P.L. 106-554). In addition, lending intermediaries receive an annual grant from the SBA to provide on-going technical assistance to small businesses. Technical assistance is a fundamental component of this program because it helps support the microlenders who teach microentrepreneurs how to manage a successful business and how to run a successful business to insure loan repayment.

As industry experts and micro-borrowers have testified numerous times, the link between financing and technical assistance is critical to the success of micro enterprise, in general, and the SBA Microloan Program in particular. Low default rates of microloans are evidence of the tremendous success of this program. Since the first SBA microloan was made in 1992, the Federal government has had only one default of its intermediary loan providers. To date, all losses incurred by intermediaries have been fully covered by the mandatory loss reserve that each intermediary must maintain. Because of this successful track record, in 1997 Congress voted to transform the Microloan Program from a demonstration program to permanent part of the array of SBA credit assistance programs.

There are currently 163 intermediaries and 19 non-lending technical assistance providers in the SBA Microloan Program. To date, the lending intermediaries have made 11,800 loans worth nearly \$122 million. The SBA reports that for every microloan, 1.7 jobs are created. The average loan to a microentrepreneur is about \$10,500, with interest rates averaging 11 percent and an average term of 39 months.

#### *Microloan borrowers—A profile*

Microentrepreneurs range from the single mother on public assistance, who borrows a few hundred dollars to buy sewing equipment and supplies to start her own alterations shop, to a mechanic who borrows a few thousand dollars to buy tools to start a repair shop.

Across the country, microloans and technical assistance are working, assisting individuals with the tools to successfully start and manage their own businesses. The SBA's Massachusetts Small Business Person of the Year for 2000 more than proves that. Lowell Gray of Lynn, Massachusetts, obtained a \$25,000 SBA microloan when his business needed it most and turned a small software company into Shore.net—an Internet service provider—with 85 employees. He sold it last year for an astounding \$43 million. In Kansas City, Missouri, the Center for Business Innovation (KC-CBI) is about to make its second loan to a microentrepreneur who was in poverty when she applied for her initial loan. Two years after her initial microloan, her revenues have gone from less than \$20,000 to \$90,000 per year, and she is ready to expand her business.

Since the microloan program was started in 1991, it has grown from 35 to 163 intermediaries. Also, the market has changed. Thus, as the Committee reviewed the program for reauthorization, it worked with trade associations representing microlenders, the Small Business Administration, and individual microlenders to craft legislation that would meet market needs and foster the success of the program.

According to Mary Mathews of the Association for Enterprise Opportunity (AEO), who participated in a Committee Roundtable entitled "SBA's SBIC and Microloan Programs" on May 12, 1999, and represented the 500 members of AEO, Congress should raise the maximum loan size of \$25,000 because it is not worth as much today as it was in 1991, when the amount was established. In fact, according to an economist at the SBA's Office of Advocacy, the value of \$25,000 in 1991 has been reduced to \$20,200 in 2000. Said another way, if a borrower took out a \$25,000 loan in 1991 and wanted to have the same purchasing power in 2000, he or she would need to borrow \$31,000 *in 2001*. Separately, the National Association of SBA Microloan Intermediaries (NASMI) has urged the Committee to increase the limit.

Subsequently, on December 21, 2000, The Small Business Reauthorization Act of 2000 (P.L. 106-554) was enacted. It included a number of important improvements to the Microloan program legislation. Chief among those changes, in large part to reflect inflation, was an increase in the maximum loan amount and average loan sizes. The maximum loan amount was increased from \$25,000 to \$35,000, the average loan size for each intermediary's portfolio was increased from \$10,000 to \$15,000. For speciality lenders, those making smaller loans and receiving additional technical assistance to make them, the legislation raised their average loan size from \$7,500 to \$10,000.

This new law also raised the threshold for the comparable credit test from \$15,000 to \$20,000. Since 1991, Microloan intermediaries have been allowed to make loans of \$15,000, but not more unless the borrower demonstrated that it was unable to get comparable credit, at comparable rates, from another area lender.

Another program change in P.L. 106-554 addressed the need for more non-lending technical assistance providers (TA providers). Prior to this change, the law limited the number of TA providers to 25 nationally, with a maximum of one per state. In a 1996 Report to Congress, SBA provided data indicating that for every dollar granted under the non-lending technical assistance program, approximately five dollars were leveraged from the private sector. At the request of the Administration, the Committee agreed to increase the number of TA providers to 55 from 25 so that there can be one from each state and the District of Columbia, Puerto Rico, the U.S. Virgin Islands, Guam, and American Samoa. In addition, to reflect the impact of inflation and increased costs, the Committee raised the maximum grant amount to each TA provider from \$125,000 to \$200,000.

During a Committee field hearing on the Microloan Program in Boston in 1998 and a Committee Roundtable in 1999, witnesses underscored the need to make the program more accessible to more borrowers across the country, whether they live in a rural or urban area. Currently, there are 163 intermediaries out of the 200 Con-

gressionally authorized. Two states—Louisiana and Wyoming—do not have any Microloan intermediaries, and an effort is underway to find appropriate participants. While inadequate appropriations for technical assistance are partially to blame for the inability of the program to grow and add intermediaries, the industry groups, local economic development leaders and the SBA asked Congress to expand the program. P.L. 106–554 not only increased the authorization level for direct microloans and technical assistance for each of the next three years to allow the program to expand, but it also increased the number of intermediaries authorized. Starting in FY2001, SBA is authorized to fund 300 intermediaries. The changes provide SBA with the tools to make this program available nationwide.

*The Microloan Program Improvement Act of 2001 (S. 174)*

By approving the “Microloan Program Improvement Act of 2001” (S. 174), the Committee adopted a number of changes to make the program more flexible. First, S. 174 would eliminate the requirement that intermediaries make “short-term” loans. This change will give intermediaries greater latitude to develop microloan products by offering their borrowers revolving lines of credit, such as for seasonal contract needs.

Second, S. 174 would broaden the eligibility criteria for intermediaries. Instead of requiring intermediaries to have one year of experience making microloans to startup, newly established or growing small businesses and providing technical assistance to its borrowers, this legislation would deem a prospective intermediary eligible if it has “equivalent experience.” SBA has nearly 10 years of experience running this program, and we expect the Agency will adopt a reasonable definition for “equivalent experience.”

Third, S. 174 would eliminate the restriction on how much technical assistance funding an intermediary can use for pre-loan assistance. Currently, intermediaries are limited to using 25 percent of their technical assistance funds to assist prospective borrowers. This change shifts the responsibility to the lender to determine how to allocate technical assistance appropriately.

Fourth, S. 174 would increase the percentage of technical assistance grant funds that an intermediary can use for subcontracting technical assistance. Currently, intermediaries can only subcontract 25 percent, and the bill would raise the threshold to 35 percent.

Lastly, as Congress expands the program and increases the number of SBA lending intermediaries around the country, the Committee wants to insure that new intermediaries benefit from lessons learned by other more experienced lending intermediaries. Due to the relative youth of the microlending industry, few conventional training resources are available to prospective and new intermediaries. According to the National Association of SBA Microloan Intermediaries, experienced SBA microlenders are called upon frequently to assist new intermediaries in addressing issues with their loan fund. The issues might range from financial management and marketing to targeting loan funds effectively to a population or business sector.

While these experienced intermediaries do their best to respond to the needs of their colleagues, they lack the resources to respond

effectively and efficiently to the growing needs of the field. S. 174 addresses that need and includes a new provision sponsored by Senators Olympia Snowe and Kerry that would establish a peer-to-peer mentoring program for SBA intermediaries and organizations seeking to become SBA microlending intermediaries. Specifically, SBA would be allowed to use up to \$1 million of its annual appropriations for technical assistance grants to subcontract with one or more national trade associations of SBA microlending intermediaries or eligible entities knowledgeable about, and experienced in, microlending and related technical assistance, to provide peer-to-peer mentoring. The Committee supports this concept because it will help make the program available nationwide, while maintaining its high quality and low loss rates.

#### II. COMMITTEE VOTE

In compliance with rule XXVI(7)(b) of the Standing Rules of the Senate, the following vote was recorded on February 28, 2001. A motion by Senator Bond to adopt S. 174, the Microloan Program Improvement Act of 2001 was approved by recorded vote, 18–0, with the following Senators voting in the affirmative: Bond, Kerry, Burns, Bennett, Snowe, Enzi, Fitzgerald, Crapo, Allen, Ensign, Levin, Harkin, Lieberman, Wellstone, Cleland, Landrieu, Edwards, and Cantwell.

#### III. EVALUATION OF REGULATORY IMPACT

In compliance with rule XXVI(11)(b) of the Standing Rules of the Senate, it is the opinion of the Committee that no significant additional regulatory impact will be incurred in carrying out the provisions of this legislation. There will be no additional impact on the personal privacy of companies or individuals who utilize the services provided.

#### IV. CHANGES IN EXISTING LAW

In the opinion of the Committee, it is necessary to dispense with the requirement of section 12 of rule XXVI of the Standing Rules of the Senate in order to expedite the business of the Senate.

#### V. COST ESTIMATE

In compliance with rule XXVI(11)(a)(1) of the Standing Rules of the Senate, the Committee estimates the cost of the legislation will be equal to the amounts discussed in the following letter from the Congressional Budget Office.

U.S. CONGRESS,  
CONGRESSIONAL BUDGET OFFICE,  
*Washington, DC, March 16, 2001.*

Hon. CHRISTOPHER S. BOND,  
*Chairman, Committee on Small Business,*  
*U.S. Senate, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for S. 174, the Microloan Program Improvement Act of 2001.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Ken Johnson.

Sincerely,

BARRY B. ANDERSON  
(For Gen. Dan L. Crippen, Director).

Enclosure.

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

*S. 174—Microloan Program Improvement Act of 2001*

S. 174 would make certain changes to the microloan program operated by the Small Business Administration (SBA). Under the microloan program, the SBA provides grants, loans, and loan guarantees to nonprofit organizations, which use the funds to provide small businesses with technical assistance and loans. The bill would amend certain restrictions in current law on how the nonprofit organizations can spend the technical assistance grants they receive under the microloan program. Also, the bill would authorize the SBA to earmark up to \$1 million for subcontracts with national trade associations to offer peer counseling for the nonprofit organizations.

Based on information from the SBA, CBO expects that the bill would not have a significant effect on the amounts authorized for technical assistance grants under the microloan program or on the rate at which funds are spent. Therefore, we estimate that S. 174 would not have a significant impact on the federal budget. Because the bill would not affect direct spending or receipts, pay-as-you-go procedures would not apply.

S. 174 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act and would not affect the budgets of state, local, or tribal governments.

The CBO staff contact is Ken Johnson. This estimate was approved by Peter H. Fontaine, Deputy Assistant Director for Budget Analysis.

VI. SECTION-BY-SECTION ANALYSIS

*Section 1.* Sets for the title of the bill, the “Microloan Program Improvement Act of 2001.”

*Section 2.* Subsection (a)(1) would eliminate the requirement that intermediaries make “short-term” loans. This change would allow Microloan intermediaries greater latitude in developing microloan products by offering their borrowers revolving lines of credit, such as for seasonal contract needs.

Subsection (a)(2) would broaden the eligibility criteria for Microloan intermediaries. Current law requires intermediaries to have one year of experience making microloans to startup, newly

established or growing small businesses and providing technical assistance to its borrowers. This provision would deem a prospective intermediary eligible if it has “equivalent” experience, which would be defined by SBA.

Subsection (a)(3) would eliminate the restriction on how much technical assistance funding an intermediary can use for pre-loan assistance. Under current law, intermediaries are limited to using 25 percent of the technical assistance to assist prospective borrowers. This provision would allow an intermediary to allocate as much of its technical assistance as it deems appropriate.

This subsection would also increase the percentage of technical assistance that an intermediary can use to contract out technical assistance. Currently, intermediaries can only contract out 25 percent; this provision would raise the limit to 35 percent.

Subsection (a)(4) would establish a peer-to-peer mentoring program for SBA Microloan intermediaries and organizations seeking to become Microloan intermediaries. This provision would allow SBA to use up to \$1 million of its annual appropriations for technical assistance grants to subcontract with one or more national trade associations of SBA Microloan intermediaries or other entities knowledgeable about, and experienced in, microlending and related technical experience to provide peer-to-peer mentoring.