441 G St. N.W.
Washington, DC 20548

August 27, 2021

The Honorable Benjamin L. Cardin
Chairman
The Honorable Rand Paul
Ranking Member
Committee on Small Business and Entrepreneurship
United States Senate

The Honorable Nydia Velázquez
Chairwoman
The Honorable Blaine Luetkemeyer
Ranking Member
Committee on Small Business
House of Representatives

Small Business Administration: Physical Disaster Loan Performance Before and After Changes in Statutory Collateral Requirements

This letter formally transmits the attached briefing slides associated with the mandate included in the Rebuilding Small Businesses After Disasters Act (see enclosure), which required GAO to submit a report comparing the performance of physical disaster loans that the Small Business Administration (SBA) made before and after the Recovery Improvements for Small Entities (RISE) After Disaster Act of 2015.

SBA provides physical disaster loans to rebuild and replace uninsured or underinsured property damaged in a declared disaster area. The President can declare a major disaster in response to a request by the governor of a state or territory or the chief executive of a tribal government. The SBA Administrator can issue a disaster declaration for an event that does not rise to the level of a presidential disaster declaration in response to a timely request by a state governor. Physical disaster loans are available to homeowners, renters, businesses of all sizes, and private nonprofit organizations. The RISE After Disaster Act of 2015 was enacted on November 25, 2015, and it amended the collateral requirements for physical disaster loans by raising the limit for unsecured loans made under SBA disaster declarations from $14,000 to $25,000.

On June 24 and 25, we provided briefings to the staffs of your committees that compared the performance of physical disaster loans issued under SBA disaster declarations before and after the RISE After Disaster Act of 2015 from January 1, 2000, to September 30, 2020. To provide this comparison, we (1) obtained data from SBA's Office of Disaster Assistance and Office of Capital Access for loans made under SBA disaster declarations from January 1, 2000, to September 30, 2020; (2) reviewed relevant federal laws and regulations and SBA policies; (3) interviewed SBA officials; and (4) performed various analytical techniques to compare the performance of loans that were approved under SBA disaster declarations before the RISE After Disaster Act of 2015 to the performance of those that were approved after the act.

The slides in the enclosure have been updated since we briefed your staffs in June 2021. Specifically, the slides were updated in August 2021 for the dates we conducted our audit and for copyediting.

We conducted this performance audit from February 2020 to August 2021 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Agency Comments

We provided a draft of this report to SBA for comment. SBA had no comments on this report.

We are sending copies of this report to the appropriate congressional committees, the Administrator of the Small Business Administration, and other interested parties. In addition, the report is available at no charge on our website at https://www.gao.gov.

If you or your staffs have any questions concerning this report, please contact me at (202) 512-9377 or clarkce@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report were Joshua Marcus (Assistant Director), Ryan Guthrie (Auditor in Charge), Michael Chacon, and Melinda Cordero. Also contributing to the report were Princess Adrineda, Breanne Cave, Justin Fisher, Maxine Hattery, John Karikari, Jason Kelly, Jason Kirwan, and Lisa Motley.

Cheryl E. Clark

Cheryl E. Clark
Director, Financial Management and Assurance

Enclosure

Enclosure I: Briefings to Senate Committee on Small Business and Entrepreneurship on June 24, 2021, and to House Committee on Small Business on June 25, 2021

GAO@100
A Century of Non-Partisan Fact-Based Work

Enclosure I

Small Business Administration (SBA) Physical Disaster Loan Performance Before and After the Recovery Improvements for Small Entities After Disaster Act of 2015

Briefing to Senate Committee on Small Business and Entrepreneurship on June 24, 2021

Briefing to House Committee on Small Business on June 25, 2021

Note: This enclosure was updated in August 2021 for the dates the audit was conducted and for copyediting.

For more information, contact Cheryl E. Clark at (202) 512-9377 or clarkce@gao.gov Page 1

GAO@100
A Century of Non-Partisan Fact-Based Work

Introduction: GAO's Mandate

- The Small Business Act authorizes SBA to make available direct physical disaster loans to help entities recover from both presidentially declared and SBA-declared disasters.[1]
- On November 25, 2015, Congress and the President enacted the Recovery Improvements for Small Entities After Disaster Act of 2015 (RISE Act), Pub. L. No. 114-88, section 2102 of which amended certain collateral requirements for physical disaster loans issued under SBA-declared disasters.
  - SBA previously amended the collateral requirements for physical disaster loans from presidentially declared disasters.
- The Rebuilding Small Businesses After Disasters Act, Pub. L. No. 116-70, § 3 (2019), includes a requirement for GAO to submit a report comparing the performance, including the default rate, of SBA physical disaster loans made from January 1, 2000, through the date on which SBA began making loans in accordance with the amendment made by the RISE Act to those made in accordance with that amendment.
- This briefing provides information collected for GAO's report in response to the mandate.

[1] 15 U.S.C. § 636(b)(1).

Page 2

GAO@100
A Century of Non-Partisan Fact-Based Work

Objective

- Compare the default and charge-off rates of physical disaster loans, with and without collateral, issued under SBA disaster declarations since the RISE Act was enacted to physical disaster loans issued prior to the act.

Page 3

GAO@100
A Century of Non-Partisan Fact-Based Work

Scope and Methodology

- Focused on physical disaster loans issued under SBA disaster declarations from January 1, 2000, through September 30, 2020.
- Reviewed relevant federal laws and regulations, as well as SBA policies and guidance.
- Interviewed SBA officials to develop an understanding of the physical disaster loan program and physical disaster loan data and the associated information systems.

Page 4

GAO@100
A Century of Non-Partisan Fact-Based Work

Scope and Methodology

- Obtained and analyzed SBA physical disaster loan data for disasters declared from January 1, 2000, through September 30, 2020.
- Calculated and compared default and charge-off rates for pre-RISE Act and post-RISE Act loans that were made under SBA disaster declarations.
  - Default rates are based on the number of loans that have ever gone into default and that SBA has placed into liquidation status, which occurs when loans are 90 days delinquent. Borrowers can catch up on payments to bring their loans out of liquidation and back to a current status.
  - Charge-off rates are based on the number of loans that SBA has determined to be uncollectible—after exhausting all reasonable efforts—and moved from liquidation to charge-off status.

Page 5

GAO@100
A Century of Non-Partisan Fact-Based Work

Scope and Methodology

- We conducted this performance audit from February 2020 to August 2021 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.
- We provided a draft of this briefing to SBA for comment. SBA did not have any comments.

Page 6

GAO@100
A Century of Non-Partisan Fact-Based Work

Background

- SBA physical disaster loans provide for the permanent rebuilding and replacement of uninsured or underinsured property damaged in a declared disaster area. They are available to homeowners, renters, businesses of all sizes, and private nonprofit organizations.

Page 7

GAO@100
A Century of Non-Partisan Fact-Based Work

Background

Physical Disaster Loans

- Provide loan terms up to 30 years.
- Lending limits:
  - $200,000 for homeowners to repair or replace primary residence; $40,000 for homeowners/renters to repair or replace personal property damaged or destroyed by the disaster.
  - $2 million for businesses or nonprofits and their affiliates for each disaster, although SBA may waive this limit in certain circumstances.
- Effective March 30, 2020, SBA provided an automatic deferment of payments until March 31, 2022, for existing borrowers of physical disaster loans that were in regular servicing status on March 1, 2020 because of the COVID-19 public health emergency.

Page 8

A Century of Non-Partisan Fact-Based Work

Background

Disaster Declaration Types and Limits

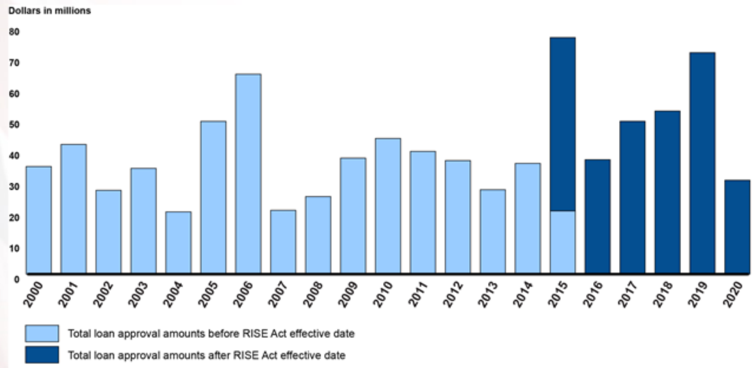
- The SBA Administrator can declare a physical disaster for an event that does not rise to the level of a presidential disaster declaration in response to a timely request by a state governor.
- Limits for loans without collateral from presidential disaster declarations were increased from $14,000 to $25,000 in 2014.
- The RISE Act temporarily provided the same increase for loans without collateral from SBA disaster declarations. The increase expires on November 25, 2022, when, absent further revision of the statute, the amount will revert back to $14,000.
- Of the $28 billion in approved SBA physical disaster loans for years 2000 through 2020, $855 million were issued under SBA disaster declarations.

Page 9

GAO@100
A Century of Non-Partisan Fact-Based Work

Background

Figure 1: Physical Disaster Loan Approval Totals from SBA Disaster Declarations from 2000 through 2020 as of September 30, 2020



Source: GAO analysis of Small Business Administration data. | GAO-21-581R

Notes: Figure represents the dollar value of Small Business Administration (SBA) loans approved by calendar year for SBA disaster declarations from January 1, 2000, through September 30, 2020. The Recovery Improvements for Small Entities After Disaster Act of 2015 (RISE Act) was enacted on November 25, 2015.
Over the past 21 years, annual loan approval totals varied from the lowest total of $20 million in 2004 to the highest of $76 million in 2015.
The RISE Act gave SBA authority to make additional disaster loans for Hurricane Sandy, which made landfall in 2012, for a period of 1 year. On December 2, 2015, SBA reopened disaster loan filing for Hurricane Sandy survivors, which resulted in a large volume of loan approvals in December 2015. Although there were presidential disaster declarations for Hurricane Sandy, the loans from this reopening were processed under SBA disaster declarations.

Page 10

GAO@100
A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Performance of Physical Disaster Loans Issued under SBA Disaster Declarations

- Pre-RISE Act default and charge-off rates are higher than post-RISE Act rates; however, as post-RISE Act loans reach a maturity level similar to that of pre-RISE Act loans, their default and charge-off rates may increase.[2]
- Pre-RISE Act loans had approximately 5 to 20 years to perform; post-RISE Act loans all had less than 5 years.
- For the pre-RISE Act loans that defaulted, an average of 53 months elapsed from the disbursement date to default date.
    - Only 12.3 percent of post-RISE Act loans had this long to perform.

[2]We cannot isolate the contribution of the RISE Act to the loan performance because there are confounding factors, such as differences in loan maturity and the state of the economy.

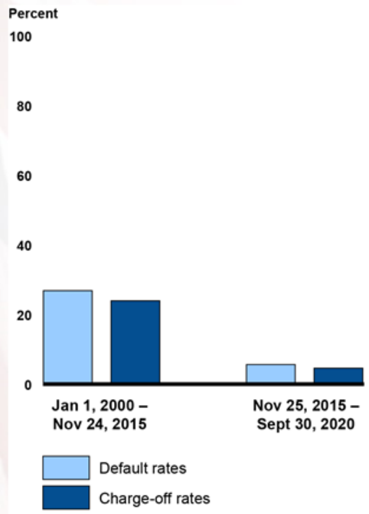
Page 11

GAO@100

A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Figure 2: Performance of Physical Disaster Loans Issued under SBA Disaster Declarations as of September 30, 2020



- Pre-RISE Act loans had a default rate of 26.8 percent and a charge-off rate of 23.9 percent.
- Post-RISE Act loans had a default rate of 5.6 percent and a charge-off rate of 4.6 percent

Source: GAO analysis of Small Business Administration data. | GAO-21-581R

Note: Figure represents Small Business Administration (SBA) loans approved for SBA disaster declarations from January 1, 2000, through September 30, 2020. The Recovery Improvements for Small Entities After Disaster Act of 2015 (RISE Act) was enacted on November 25, 2015.

Page 12

GAO@100
A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Performance of Physical Disaster Loans Issued under SBA Disaster Declarations—Uncollateralized Compared to Collateralized

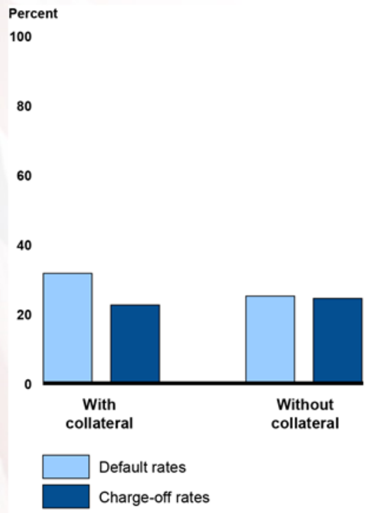
- Loans with collateral did not necessarily perform better than loans without collateral.
- Since post-RISE Act loans had less than 5 years to perform, default and charge-off rates may increase for these loans regardless of whether they have collateral.

Page 13

GAO@100
A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Figure 3: Performance of Physical Disaster Loans Issued under SBA Disaster Declarations Before the RISE Act as of September 30, 2020



- Loans with collateral had a default rate of 31.6 percent and a charge-off rate of 22.5 percent.
- Loans without collateral had a default rate of 25.1 percent and a charge-off rate of 24.4 percent.

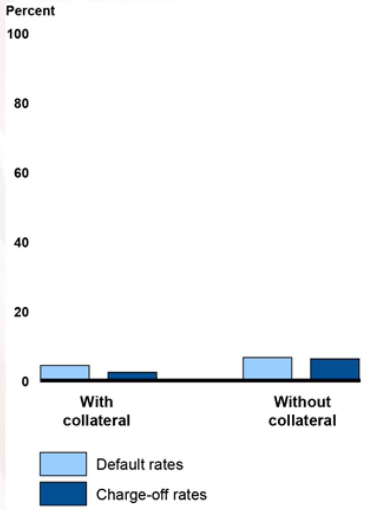
Source: GAO analysis of Small Business Administration data. | GAO-21-581R

Note: Figure represents Small Business Administration (SBA) loans approved for SBA disaster declarations from January 1, 2000, through November 24, 2015. The Recovery Improvements for Small Entities After Disaster Act of 2015 (RISE Act) was enacted on November 25, 2015.

Page 14

Physical Disaster Loan Performance

Figure 4: Performance of Physical Disaster Loans Issued under SBA Disaster Declarations After the RISE Act as of September 30, 2020



- Loans with collateral had a default rate of 4.4 percent and a charge-off rate of 2.4 percent.
- Loans without collateral had a default rate of 6.6 percent and a charge-off rate of 6.2 percent.

Source: GAO analysis of Small Business Administration data. | GAO-21-581R

Note: Figure represents Small Business Administration (SBA) loans approved for SBA disaster declarations from November 25, 2015 through September, 30, 2020. The Recovery Improvements for Small Entities After Disaster Act of 2015 (RISE Act) was enacted on November 25, 2015.

GAO@100
A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Performance of Physical Disaster Loans Issued under SBA Disaster Declarations—Other Factors

- Other factors that may also affect performance, include:
  - Changes in SBA's lending practices, such as a change in 2014 to consider applicants credit scores and credit history.
  - Economic conditions in a given disaster area.
  - Payment deferrals beginning in March 2020 because of the COVID-19 public health emergency.

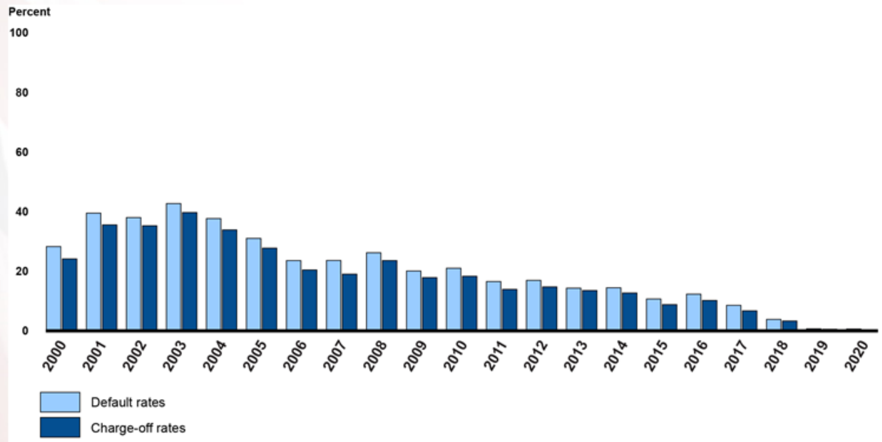
Page 16

GAO@100

A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Figure 5: Performance of Physical Disaster Loans Issued under SBA Disaster Declarations as of September 30, 2020



Source: GAO analysis of Small Business Administration data. | GAO-21-581R

Notes: Figure represents Small Business Administration (SBA) loans approved by calendar year for SBA disaster declarations from January 1, 2000, through September 30, 2020. SBA lending policies have varied over the 20 year period.
Older loans have had more time to perform and as a result generally have higher default and charge-off rates.

Page 17

GAO@100
A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Performance of Physical Disaster Loans Issued under SBA Disaster Declarations over 4 Years

- To minimize the effects of having large differences in the age of loans, we compared default and charge-off rates during the first 4 years of the following:
  - Pre-RISE Act loans disbursed from January 1, 2011, through November 24, 2015
  - Post-RISE Act loans disbursed from November 25, 2015, through September 30, 2020
- The default and charge-off rates for each year varied by less than one percentage point.
- Consistent with the overall 20 year trend previously shown, default and charge-off rates will likely increase as the loans mature.

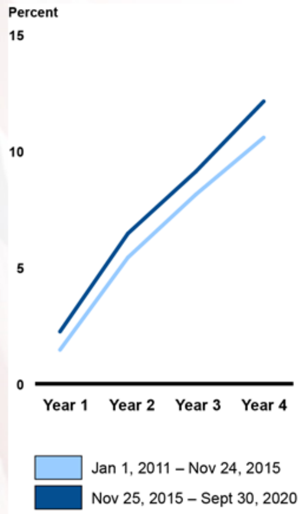
Page 18

GAO@100

A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Figure 6: Default Rates of Physical Disaster Loans Issued under SBA Disaster Declarations over 4 Years as of September 30, 2020



- The default rates varied by less than one percentage point for each year and less than two percentage points cumulatively.

Source: GAO analysis of Small Business Administration data. | GAO-21-581R

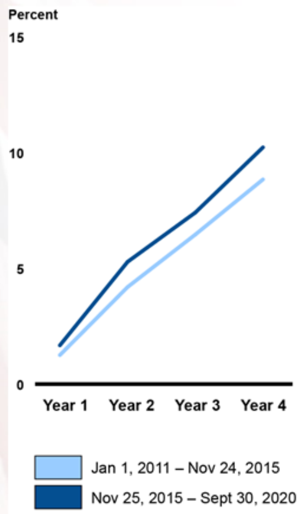
Note: Figure represents Small Business Administration (SBA) loans approved for SBA disaster declarations from January 1, 2011, through November 24, 2015 and from November 25, 2015, through September 30,2020. The Recovery Improvements for Small Entities After Disaster Act of 2015 (RISE Act) was enacted on November 25, 2015.

Page 19

GAO@100
A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Figure 7: Charge-off Rates of Physical Disaster Loans Issued under SBA Disaster Declarations over 4 Years as of September 30, 2020



- The charge-off rates varied by less than one percentage point for each year and less than two percentage points cumulatively.

Source: GAO analysis of Small Business Administration data. | GAO-21-581R

Note: Figure represents Small Business Administration (SBA) loans approved for SBA disaster declarations from January 1, 2011, through November 24, 2015 and from November 25, 2015, through September 30, 2020. The Recovery Improvements for Small Entities After Disaster Act of 2015 (RISE Act) was enacted on November 25, 2015.

Page 20

GAO@100
A Century of Non-Partisan Fact-Based Work

Physical Disaster Loan Performance

Summary

- For loans approved under SBA disaster declarations, pre-RISE Act default and charge-off rates are higher than post-RISE Act rates; however, as post-RISE Act loans reach a maturity level similar to that of pre-RISE Act loans, their default and charge-off rates may increase. [3]
- Pre-RISE Act loans had approximately 5 to 20 years to perform; post-RISE Act loans all had less than 5 years.
- An analysis of the first 4 years of both pre-RISE Act and post-RISE Act loans showed that the default and charge-off rates varied by less than one percentage point for each of the years.
- Loans with collateral did not necessarily perform better than loans without collateral.
- Other factors, such as changes in SBA's lending policies and the COVID-19 payment deferral, could also affect loan performance.

[3]We cannot isolate the contribution of the RISE Act to the loan performance because there are confounding factors such as differences in loan maturity and the state of the economy.

(104077)

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through our website. Each weekday afternoon, GAO posts on its website newly released reports, testimony, and correspondence. You can also subscribe to GAO's email updates to receive notification of newly posted products.

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, https://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on Facebook, Flickr, Twitter, and YouTube.
Subscribe to our RSS Feeds or Email Updates. Listen to our Podcasts.
Visit GAO on the web at https://www.gao.gov.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact FraudNet:

Website: https://www.gao.gov/about/what-gao-does/fraudnet

Automated answering system: (800) 424-5454 or (202) 512-7700

Congressional Relations

A. Nicole Clowers, Managing Director, ClowersA@gao.gov, (202) 512-4400, U.S. Government Accountability Office, 441 G Street NW, Room 7125, Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Strategic Planning and External Liaison

Stephen J. Sanford, Managing Director, spel@gao.gov, (202) 512-4707
U.S. Government Accountability Office, 441 G Street NW, Room 7814,
Washington, DC 20548