

## ANALYSIS OF FINANCIAL RESULTS

This is the 15th year that the Small Business Administration has issued audited Agency-wide financial statements. These financial statements have been prepared in accordance with guidance issued by the Office of Management and Budget (OMB) pursuant to the Chief Financial Officers (CFO) Act of 1990. The Introduction to the Financial Statements and the Notes to the Financial Statements in this report provide more details on the SBA's financial results and the preparation of the financial statements.

### **Background**

The SBA is the smallest of the major Federal credit agencies, behind the Department of Agriculture, Department of Education, the Department of Housing and Urban Development and the Department of Veterans Affairs. However, unlike the other major Federal credit agencies, virtually 100% of the SBA's FY 2005 \$3.9 billion budgetary appropriations is devoted to lending.

At September 30, 2005, the SBA had guaranteed \$61.1 billion of loan principal, up 8% from September 30, 2004. The SBA's portfolio of loans receivable also continued to grow, valued at \$4.3 billion this year, an increase of 25% over last fiscal year. The loan portfolio includes defaulted guaranteed loans as well as loans made directly to the victims of natural disasters and in the Agency's MicroLoan Direct program.

The SBA's assets and liabilities are primarily the result of its credit program activities, and include: fund balances with Treasury, credit program receivables, liabilities for loan guaranties, Treasury debt and other asset and liability accounts. The SBA's loans and guaranties are financed by a combination of two sources: one for the long-term cost of the loan and another for the remaining non-subsidized portion of the loan. Congress provides appropriations to cover the estimated long-term costs of SBA loans, which are defined as the net present value of the estimated cash outflows and inflows associated with the loans. The remaining portion of each direct loan that does not represent long-term cost is financed under permanent indefinite borrowing authority to borrow funds from the U.S. Department of the Treasury.

Credit program receivables for the SBA are composed of disaster direct loans and defaulted business loans purchased per the terms of the SBA's loan guaranty programs.

### **Financial Position**

#### **Assets**

The SBA had total assets of \$11.9 billion at the end of FY 2005, up 12.7% over FY 2004. Assets increased primarily due to an increase in fund balance with Treasury and an increase in the net book value of credit program receivables. Most credit program receivables are valued at the present value of expected future cash flows, per the provisions of the Federal Credit Reform Act of 1990. The

increase in Fund Balance with Treasury was primarily a result of an increase in unexpended appropriations. The increase in credit program receivables reflects the Agency's increased disbursements of disaster loans, up 115.0% over FY 2004, as well as purchases of guaranteed business loans. Both activities increased the loan portfolio by a greater amount than borrower repayments decreased already-existing SBA-owned direct and previously-purchased loan principal amounts.

### Liabilities

The SBA had total liabilities of \$11.3 billion at the end of FY 2005, down 7.2% over FY 2004. Liabilities consist primarily of the Liability for Loan Guaranties, an estimate of the future amount the SBA will pay, net of fee collections, to liquidate expected purchases of guaranteed loans under its guaranty loan programs, and Debt with Treasury, borrowed primarily to disburse loans under direct loan programs. Both are down, FY 2005 compared to FY 2004, because the subsidy costs of the SBA's loan programs, broadly, are decreasing.

### Net Position

Net position, the sum of Unexpended Appropriations and Cumulative Results of Operations, increased in FY 2005 to \$617.6 million. Unexpended Appropriations increased due to emergency appropriations for hurricane relief received in FY 2005. Cumulative Results of Operations increased as well, due to the receipt of FY 2004 previously unfunded subsidy reestimates in FY 2005 and the lesser net amount of unfunded subsidy reestimates at the end of FY 2005.

### Results of Operations

Each year, the estimated long-term costs of the SBA's loans are reestimated for each major loan program. Reestimates update original loan program cost estimates, which are primarily due to expected defaults, to reflect actual experience and changes in forecasts of future cash flows. Increased reestimated costs are funded in the following year by permanent indefinite authority, while decreased costs are forwarded by the SBA to a special receipts fund with Treasury.

For FY 2005, the SBA recorded net downward reestimates of \$78.0 million as a reduction of net cost on the Statement of Net Cost. For FY 2004, in contrast, net cost was increased by net upward reestimates of \$806.0 million for all reestimated programs. Net Cost of Operations for 2005 and 2004 was \$807.8 million and \$1,747.6 million, respectively. Reestimates decreased by \$884.0 million between the two years, while Net Cost of Operations decreased \$939.8 million. Therefore, other administrative and programmatic costs decreased by \$55.8 million, net of revenues, from \$941.6 million to \$885.8 million.

The SBIC Participating Securities Program and the 504 Certified Development Program recorded the greatest dollar amount of reestimates at the end of FY 2005, with \$300.6 million downward and \$189.6 million downward, respectively. Both programs showed improved performance and lessening purchases necessary under the SBA's guaranties. The Disaster Loan Program recorded a relatively minor, given the program size, upward reestimate of \$44.3 million. This reflects the stability of both the program and its current subsidy model and assumptions.

The Disaster Loan program delivered an increased number and dollar amount of disaster loans to individuals and businesses in FY 2005 compared to FY 2004. The SBA disbursed \$465.2 million of disaster loans in FY 2004 and \$998.1 million in FY 2005, a 115.0 % increase. This was due to hurricanes that struck Florida in September of FY 2004, resulting in emergency disaster relief appropriations that funded both FY 2004 and increased FY 2005 disbursements. The SBA expects an even larger amount of disaster loans will be disbursed in FY 2006, due to the effects of hurricanes Katrina and Rita.

### Credit Management

The SBA has extensive debt servicing and collection practices to ensure maximum recovery. Potential borrowers must disclose delinquent government debt. Credit reports identify delinquent debtors as well, and they may be barred from obtaining SBA guaranteed loans. The Agency actively uses Federal salary offset and conducts annual matching of delinquent debtor records for civilian and military Federal employees and retirees with the Department of Defense. All loan applicants must disclose their taxpayer identification number.

Debt servicing and collection procedures include the acquisition and sale of collateral through the liquidation process, along with the vigorous pursuit of guarantors and other loan obligors.

Additionally, the SBA submits delinquent debt to the Treasury Cross-servicing Program, a centralized debt collection program administered by the Financial Management Service. Federal tax refunds, salary and retirement pay, social security benefits and other disbursements that would otherwise be paid to a delinquent borrower may be offset and remitted to the SBA for application to loan amounts outstanding.

Finally, through the Office of Lender Oversight, the Agency rates and ranks lenders disbursing SBA-guaranteed loans according to risk. Larger lenders are subject to on-site reviews. The risk analysis of lenders allows the SBA to focus resources on those lenders representing the most risk in terms of exposure and credit quality.

Certain cumulative information about loan disbursements, charge offs, and recoveries by specific loan program, both direct and guaranteed, as well as a schedule summarized for all business loans, is available at [www.sba.gov/cfo/reports.html](http://www.sba.gov/cfo/reports.html).