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Congress of the United States
U.S. House of Representatives
Committee on Small Business

2361 Rayburn House Office Building
Washington, DC 20515–6315

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The Honorable John M. Spratt, Jr
Chairman
Committee on the Budget
Room 309 Cannon HOB
Washington, DC 20515

Dear Chairman Spratt:

I am writing to advise you of the views and estimates of the Committee on Small Business with regard to the President's Fiscal Year 2009 budget proposal. While there are many agencies, programs, and initiatives within the federal government that directly or indirectly benefit or assist small business, this letter will focus on the President's FY 2009 budget request for the Small Business Administration (SBA or agency) and programs created by the Small Business Act and the Small Business Investment Act. These programs are included in the 370 Commerce and Housing Credit budget account.

OVERVIEW

The submission of the agency's budget comes during a time when the economy is sliding towards a potential recession. This downturn, due in part to the tightening of credit standards by financial institutions, will likely have a significant effect on small businesses. The economic decline is one byproduct of the growing weakness in the housing market, with an increase in foreclosures of 75 percent from 2006. The economy is also experiencing a widespread "credit crunch," as interest rates have increased by 3 percent in 3 years, which will raise the price of capital for small firms, causing many to forgo important purchases or expansion. This dampening effect has the potential to reduce entrepreneurial activity in the short-term.

Other data also shows the challenges facing the economy. Inflationary pressures remain a concern, as the U.S. saw large gains in consumer prices. The price of oil, which surpassed $100 per barrel in December, averaged $91.37 for the month, up $11.44 for the quarter and nearly $30 for the year. In recent days, it has surpassed $100 once again. Employee benefit costs outstripped gains in employee wages and salaries. The public remained somewhat pessimistic in the fourth quarter according to both the National Federation of Independent Business's optimism index and the University of Michigan's consumer sentiment survey. Finally, the service sector has weakened dramatically in January – with the ISM index plunging to 41.9 percent, the second lowest result on record.

In response to the weakening economy, the Federal Reserve has altered monetary policy to prevent recession while Congress enacted a stimulus package to increase consumer demand and the flow of capital. However, the Small Business Administration has failed to utilize its budget submission to strengthen the small business component of the economy.

The SBA's FY 2009 budget proposes funding for the agency's core programs, on-going operating expenses, continuing modernization efforts and assistance for small businesses impacted by disasters. The Administration's SBA budget recommends funding the agency at $482 million. Funding will be cut by nearly $86 million, or 15 percent, compared to what was provided last year. And since this Administration took office, the proposed SBA budget has seen an overall cut of 50 percent.

The FY 2009 budget requests no funding for the Microloan technical assistance program, the Program for Reinvestment for Microentrepreneurs (PRIME), the New Markets Venture Capital program, the Small Business Investment Company participating securities program, BusinessLINC, the Small Business Innovation Research (SBIR) Federal State and Technology Partnership Program, and the SBIR Rural Outreach Program.

SBA's proposal continues to consolidate agency services by shifting the costs of several programs into the salary and expense (S&E) line item. The programs centralized into S&E include: Advocacy Research ($11 million), National Ombudsman ($1.5 million), 7(j) technical assistance ($1.5 million), HUBZones ($2 million), and Native American Outreach ($1 million). As a result, the transparency of the agency's budget submission is greatly reduced, making it very difficult for Congress to analyze the agency's priorities and what programs it intends to focus resources.

LENDING PROGRAMS

The Disaster Loan Program – The SBA's Disaster Assistance Program is responsible for providing affordable, timely and accessible financial assistance to homeowners, renters and businesses following a disaster. Financial assistance is available in the form of low-interest, long-term loans and is the primary form of federal assistance for the repair and rebuilding of non-farm, private sector disaster losses. For this reason, the disaster loan program is the only form of SBA assistance not limited to small businesses. Current law provides a four percent interest rate to disaster loan borrowers who do cannot access credit elsewhere.

For FY 2009 the SBA requests only $14.3 million in new funds for disaster loan making, expecting to once again fund the bulk of its loan making with carryover funds received through emergency appropriations in prior fiscal years. Additionally, the total amount of loan making authority for FY 2009 is commensurate with the agency's "normalized" 10-year average of disaster lending, which excludes major disasters such as the 1994 North Ridge Earthquake and the 2005 Gulf Coast Hurricanes.

The Committee remains concerned that the agency has not allocated any resources to implement recognized disaster readiness initiatives as recommended by the Government Accountability Office (GAO). The SBA has allocated no resources to perform disaster simulations or catastrophe modeling and has budgeted no funds to remedy the logistical and workforce deficiencies that were identified in GAO reports and Committee hearings held in the wake of the 2005 Hurricanes. The Committee therefore urges that the SBA be allocated enough funding for the loan making function to remedy improper loan cancellations and to fund the disaster loan administration function with sufficient resources to implement necessary logistical, workforce, and disaster readiness improvements. The Committee recommends that \$10 million be allocated for these purposes.

The Committee remains dismayed that the amount allocated for disaster loans and disaster administration is insufficient. For FY2009, the SBA will fund its disaster loan making with \$149.8 million carried over from funds that were originally appropriated to assist in the recovery from the 2005 Gulf Coast Hurricanes. The Committee believes that this carryover will not provide sufficient funding for the loan making function, particularly given the recent discovery of several thousand loans that were improperly canceled by the SBA in an effort to clear the massive backlog experienced in the wake of the 2005 Gulf Coast Hurricanes. Additionally, although the agency's budget will support a \$1.06 billion disaster loan level, this figure does not account for the costs of major disasters. Unlike other disaster management agencies, the SBA has not budgeted to build a contingency fund to respond in the event of a major disaster. Consequently, the Committee is concerned that the SBA remains overly dependent upon ad hoc appropriation requests and is not prepared to respond to a major disaster.

7(a) Loan Guarantee Program – The 7(a) Loan Program is the SBA's primary business loan program. The 7(a) program provides loan guarantees to eligible small businesses that have been unable to obtain financing through the private sector because commercial lenders cannot provide these loans for the purpose, in the amount, or on terms that small business borrowers require. The program relies on private-sector lenders to provide loans that are then guaranteed by the SBA. The proceeds from a 7(a) loan may be used for virtually any business purpose, including inventory, equipment, or operating expenses.

While the Federal Reserve's Senior Loan Officers' Survey reveals that the tightening of lending standards is occurring, the SBA has not taken any policy actions to make its financing programs more affordable. For FY 2009, the Administration has requested no budget authority for the 7(a) program. Instead, the Administration will continue to fund the program through fees that the SBA charges borrowers and lenders. Since FY 2005, these borrower and lender fees have dramatically increased costs for 7(a) loans and are likely contributing to the recently observed decrease in lending volume and lender participation in the 7(a) program.

For FY 2009, the SBA has proposed to again raise the ongoing annual lender fee to the statutory maximum level of 0.55 percent, over twice the fee charged only five years earlier. At the same time, the agency makes no proposal to lower the fees levied on borrowers in the 7(a) program. Fees on smaller loans will remain twice the amount charged five years ago and for mid-sized loans, fees have increased 20 percent in the same time period. For some borrowers, the upfront guarantee fee can be in excess of $50,000, this is in addition to the ongoing annual fees charged to the lender. In raising fees to their maximum statutory levels, the agency has brought has the program to the brink of shutdown – leaving little room to absorb unforeseen costs. The Committee recommends that additional steps be taken to make these loans affordable and accessible to the small businesses the program was originally intended to serve and allow for growth of the program to a $20 billion loan level for FY 2009. For these purposes, the Committee recommends that an appropriation of $150 million be made available.

These increases in borrower and lender fees have begun to adversely affect the program's loan volume. In FY 2006, the program experienced a 3 percent decline in loan volume from the previous year. This was the first time in over a decade that loan volume decreased from one fiscal year to the next. Unfortunately, this trend continued unabated in FY 2007, with loan remaining 2.4 percent below its FY 2005 level. Nor does this trend appear to be over, as already in quarter of FY 2008 7(a) lending has declined by 14 percent in number of loans and almost 6 percent in total amount of loans compared to the same time in 2007. Lending to minority owned businesses has declined almost 9 percent in both number of loans and total dollars, and SBA Express (the agency's largest program in pure volume of 7(a) loans) is down 24 percent in number of loans and 21 percent in total dollars compared to this time last year.

Even as loan volume has fallen, the program has experienced a steady decline in average loan size from $236,280 in FY 2002 to $143,000 in FY 2007. Despite the fact that operating costs for businesses have increased throughout the same period, the 7(a) program has been providing businesses with smaller loans, leaving many businesses unable to secure capital necessary to meet increasing costs and grow their business.

Finally, the SBA also continues to lose ground in attracting new lenders to participate in the 7(a) program. In FY 2007, only 2,374 lenders participated in the 7(a) program. This represents more than a 16 percent decline in the number of lenders from FY 2003 when 2840 lenders participated in the program. While a good deal of this decline may be attributable to the discontinuation of the LowDoc program in FY 2005, much of the cause may stem from the challenges that small lenders have in entering the program, meeting compliance costs associated with SBA's loan regulations, and paying increased lender fees.

The FY 2009 budget does nothing to address these problems and will, in fact, exacerbate several of the program's existing deficiencies. The Administration requests a loan level of $17.5 billion for the 7(a) program, which includes funds for the SBA Express, and Community Express programs, as well as other programs operated under the 7(a) framework. The proposal is the same as its requests for FY 2007 and FY 2008.

The agency makes no proposals that would reduce the costs that borrowers and lenders incur to access the program. In fact, in FY 2009 the SBA will implement a new lender oversight initiative that will significantly increase program costs paid by lenders, in some cases by more than $30,000 per year. More notably, the Administration has taken the position that provisions in PL 110-140 and H.R. 4253 that reduce the cost of borrower fees for certain 7(a) loans are unfunded mandates that require an appropriation. It was the intent of the Committee, as reflected in the plain language of these laws, however, that these programs would continue to function within the existing zero-subsidy framework of the 7(a) program. For these reasons, the Committee remains concerned about SBA's largest loan program. The Committee expects the agency to immediately take action to implement the initiatives contained in PL 110-140 and H.R. 4253.

The 504 Certified Development Company Program – The Certified Development Company Program (also known as the 504 Loan Program) provides permanent, fixed rate financing for businesses to acquire industrial or commercial buildings or heavy equipment and machinery. Local Certified Development Companies (CDCs) working in partnership with private lenders and the SBA deliver the program for projects in the community. Typically, a 504 project includes a loan secured with a senior lien from a private-sector lender covering up to 50 percent of the project cost, a loan secured with a junior lien from the CDC (backed by a 100 percent SBA guaranteed debenture) covering up to 40 percent of the cost, and a contribution of at least 10 percent equity from the small business being helped. The 504 program differs from the 7(a) loan program, which provides variable rate, shorter term financing for general business needs.

For FY 2009, the Administration proposes a $7.5 billion program level for the CDC/504 Program. This program level is the same as was proposed in FY 2007 and FY 2008. In FY 2009, however, the SBA should begin implementation of provisions in PL 110-140 that expand the 504/CDC program to accommodate financing for projects that improve energy efficiency. The Committee feels that given the growth of this popular program and the new initiatives in PL 110-140, $9 billion in authority represents a better program level and provides a sufficient program level cushion that allows for increased program expansion.

The SBA projects that defaulted loans will increase in FY 2009 while net recoveries are projected to decline. Although this is not unexpected during an economic slowdown, the Committee expects the SBA to take additional steps to increase its liquidation and recovery efforts for loan defaults in the 504 loan program. The Committee is concerned that the FY 2009 budget does not allocate sufficient resources to provide 504 Loan Servicing Centers with sufficient staff to handle the increased defaults. The Committee also notes that the subsidy model results submitted in the budget do not account for the statutory requirement for the SBA to reimburse CDCs for their costs in recovering defaulted 504 loans. Additionally, the Administration projects that the 504 program will operate at a negative subsidy rate for FY 2009 – thus returning a surplus of funds to the federal government. The Committee therefore recommends that the agency take immediate steps to lower the fees charged program participants or use this excess revenue to offset participants' programmatic costs.

The 7(m) Microloan Program - The Microloan Program provides very small loans to start-up, newly established, or growing small business concerns. Under this program, the SBA makes funds available to nonprofit community based lenders (intermediaries) which, in turn, make loans to eligible borrowers in amounts up to a maximum of $35,000. The average loan size is about $13,000. Applications are submitted to the local intermediary and all credit decisions are made on the local level.

The maximum term allowed for a Microloan is six years. However, loan terms vary according to the size of the loan, the planned use of funds, the requirements of the intermediary lender, and the needs of the small business borrower. Interest rates vary, depending upon the intermediary lender and costs to the intermediary from the U.S. Treasury. Generally these rates will be between 8 eight percent and thirteen percent.

In FY 2007, the program provided $19 million in loans at a total cost of just $2 million and $12.8 million in technical assistance. This represented a 1.5 percent increase in lending volume over FY 2006. As it had in FY 2008, however, the Administration again proposed moving the Microloan program to a zero-subsidy policy in its FY 2009 budget. To facilitate this proposal, the SBA would significantly increase the interest rate charged to program participants for Microloan funds and would eliminate the technical assistance aspect of the program. Currently, intermediaries can borrow funds at rates as low as two percent below the five-year Treasury rate. The proposed zero-subsidy policy would require intermediaries to pay 1.3 percent over the five-year Treasury rate, a net increase of 3.3 percent. The Committee notes that this change could raise the cost to borrowers over the life of the loan by as much as $4,000 per year. The Committee believes the restructuring of the Microloan program is unwarranted. Pursuing a zero-subsidy policy in the Microloan program would likely have the same negative results as were observed when the 7(a) program was moved to a zero-subsidy policy, with significant cost increases for borrowers and lenders, smaller loan size, falling loan volume, and declining lender participation. In short, this policy would make successful loan program less affordable and less accessible for small businesses. Consequently, the Committee recommends funding be continued for the 7(m) Microloan program at a program level sufficient to support $30 million in lending.

The SBA's proposal also recommends eliminating the Microloan technical assistance (T.A.) funds, leaving the program's borrowers to rely upon assistance from the agency's network of T.A. providers (SBDC's, WBC's and SCORE). As an initial observation, the Committee notes that few intermediaries would be willing to participate in the Microloan program without real technical assistance element. Additionally, because the Administration has proposed reduced or flat-funding for all of its other T.A. programs, the Committee harbors serious doubts that either existing T.A. providers or Microloan borrowers would be well served by their combination. Consequently, the Committee recommends continued funding for technical assistance for 7(m) at $20 million to cover growth in the program.

The Small Business Investment Company (SBIC) program – The SBIC program was created to fill the gap in capital markets for long-term financing of smaller, growth-oriented domestic small businesses. Like many of the SBA's financing programs, the SBIC program operates as a public-private partnership. The SBA does not make direct investments in small business concerns through the SBIC program, but instead licenses Small Business Investment Companies (SBICs) to administer the program. SBICs are state-chartered entities organized solely for the purpose of providing a source of capital for small business concerns. SBICs with expertise in certain sectors or industries are licensed by SBA and then use their own funds, plus resources borrowed with an SBA guaranty or "leverage," to invest in small businesses. Although subject to SBA regulation, SBICs remain privately owned and managed and make their own decisions about which small businesses investments to make.

The SBA provides leverage to SBICs in two forms, "debentures" and "participating securities." To obtain leverage, SBICs issue debentures or participating securities which are guaranteed by the SBA. Separate pools of either SBA-guaranteed debentures or participating securities are formed and sold to investors through periodic securities offerings. An SBIC's business plan and investment strategy are the primary factors in determining the type of leverage used by the SBIC.

By their nature, debenture SBICs focus on companies that are mature enough to make current interest payments on the investment so that, in turn, the SBIC can meet its interest obligations on its SBA-guaranteed debentures. Thus, debenture financing will generally be best suited if the SBIC plans to invest in portfolio companies with the ability to service debt. By contrast, participating securities SBICs are able to invest equity capital in earlier stage businesses because interest is accrued on their SBA-guaranteed obligation. Thus, participating securities are well suited for SBICs investing in seed and early stage businesses or businesses that either do not have established cash flow or need to use available cash for other purposes.

The cost of the SBIC program, similar to that of the 504 Program, is supported entirely from fees – meaning that no appropriation is required. For FY 2009, the SBA budget proposes a $3 billion program level for the SBIC debenture program. This funding level is no greater than the Administration's FY 2007 budget. As it has since 2005, the SBA does not request a program level for the SBIC participating securities program, choosing instead to keep this important program shuttered. The Committee believes this is a significant mistake on the part of the Administration.

By eliminating the participating securities program, the SBA has become completely reliant on debt-based programs, which are more suited to providing later stage, expansion capital to cash-flow-positive businesses. This has particularly hampered investment in early-stage and capital-intensive small businesses, which lack the resources to service heavy debt investment. In FY 2002 the SBA licensed 41 new SBIC funds, more than half of which were for early stage investment. By contrast, in 2007 the SBA licensed only 9 new SBIC funds, none of which were for investment in early stage businesses.

In FY 2009 the SBA should begin implementation of provisions in PL 110-140 that provide for the creation of energy saving debentures in the SBIC program and establish a new Renewable Fuel Capital Investment program. The Administration has taken the position that the investment provisions in PL 110-140 are unfunded mandates that require an appropriation. The plain language of the law, however, reflects the intent of the Committee and of Congress that the investment programs established in PL 110-140 be carried-out under a zero-subsidy framework, thus negating the need for an appropriation. Consequently, the Committee expects the agency to immediately take action to implement the initiatives contained in PL 110-140. Additionally, the Committee believes that the SBA's investment programs should resume their focus on early-stage and startup business investment. For these reasons, the Committee recommends that additional steps be taken to increase the amount of equity capital provided to small businesses and allow for growth of the SBIC program to a $4 billion in debentures for FY 2009.

The New Markets Venture Capital Company (NMVC) – Congress created the New Markets Venture Capital (NMVC) program in December 2000 under the purview of the U.S. Small Business Administration (SBA) to address the unmet equity needs of low-income communities. The NMVC program was modeled after the SBA's Small Business Investment Company (SBIC) program, but was established with the specific purpose of providing economic development in low-income (LI) areas. Through a combination of equity-type financing and technical assistance to small businesses located in LI areas, the program seeks to assist local entrepreneurs, create quality employment opportunities for residents and build wealth within these communities.

Like the SBIC debenture program, the NMVC program operates as a public-private partnership between the SBA and licensed New Markets Venture Capital Companies (NMVCCs). The SBA does not make direct investments in small business concerns through the NMVC program. Instead, the SBA provides funding to NMVCCs, which then use their own funds, plus leverage borrowed with an SBA guaranty, to make investments in smaller enterprises defined by SBA regulations that are located in LI geographic areas.

Although subject to SBA regulation, NMVCCs remain privately owned and managed and make their own decisions about which small businesses investments to make, within the constraints of NMVC statute, SBA regulations, and the terms of the NMVCC's participation agreement and Operational Assistance Grant award. In this sense, the SBA's role is essentially the same as with the SBIC program. The Agency selects participants for the NMVC program, provides funding for their investments and operational assistance activities, and regulates their operations to ensure that public policy objectives are being met. The SBA requires NMVCCs to provide regular performance reports and have annual financial examinations by SBA.

The SBA arranges funding for the debentures under procedures similar to those utilized in the SBIC program. The SBA supplements NMVCC's available capital through guarantees of debentures issued by the company in a face amount of up to 1.5 times its capital. The debentures have a term of up to 10 years from the date of draw-down and are issued at a discount. Interest in the first five years is paid up front in the form of the discount, and is only payable for years 6-10. Principal is due at the end of year 10. The debentures are priced at a current market rate for comparable U.S. Government Treasury securities plus a small premium. The debentures are pre-payable without penalty after one year, and there are no SBA fees associated with the debenture.

One crucial advantage that the NMVCCs enjoy over SBICs is the addition of SBA administered operational assistance grants (OA). The SBA also will match the resources that the NMVCC has raised for operational assistance (whether in cash or in-kind) with an equivalent grant. The NMVCC must use the grant funds and matching resources to provide marketing, management and other operational assistance to the businesses in which it invests or intends to invest. In principle, the program was intended to permit NMVC companies may use capital raised with New Markets Tax Credit allocations to meet the NMVC private capital match.

In FY 2001 Congress appropriated $150 million of debenture guaranty authority and $30 million in for Operational Assistance (OA) grants to supplement the private capital that is raised by NMVC companies and Specialized Small Business Investment Companies (SSBICs), which are SBICs that specifically make loans to businesses run by socially or economically disadvantaged people and can thus participate in the NMVC program.

Beginning in 2003, however, the Administration eliminated funding for the NMVC program. For FY 2009, and consistent with its previous budget request, the SBA has again failed to request any funding for the NMVC program. As a result, the SBA has been unable to bring new NMVC companies into the program, limiting the availability of equity financing to entrepreneurs located in low-income areas. For this program to realize its full potential, the Committee supports sufficient funding to guaranty $30 million in debentures under the program and provide $5 million in operational assistance grants.

GOVERNMENT CONTRACTING PROGRAMS

Federal procurement initiatives are crucial to small businesses in an economic slowdown such as the country is experiencing now. In these unstable conditions, corporate America tends to reduce its supplier base, with small firms experiencing the first effects. Small business contracting programs are particularly critical as federal contracting dollars are on the rise. In fiscal year 2006, the Department of Defense purchased more than the entire federal government did only five years earlier. Given this, it is clear that small business access to federal contracts is more important now than ever.

The primary public policy rationale for federal small business contracting programs is the positive economic benefits they provide. These benefits can be seen in two primary areas – market competition and local economic development. First, programs that are designed to increase the number of small contractors expand the federal supplier base. This leads to increased competition, which results in higher quality, greater product variety, and lower prices. Second, these contracting initiatives lower barriers to entry in a wide range of markets. This creates greater market access for small firms' producing goods and/or providing services. From an economic perspective, such access is critical to generating positive macroeconomic benefits, including higher job creation, wage growth, and greater income distribution.

The 8(a) Program – Approaching its 40th year in 2009, the 8(a) program continues to be the main way that minority entrepreneurs enter the federal marketplace. The 8(a) program promotes individual minority entrepreneurship through the award of federal contracts. SBA assists small businesses in identifying suitable contract opportunities and then accepts and supports the performance of the awarded contract. The Administration's FY 2009 budget request for the operation of this program is $35,952,000.

In the last five years there has been an explosion of new participants accepted into the program putting more strain on an already inadequate support system and almost doubling the number of those relying on SBA for assistance. The SBA's Inspector General has listed the 8(a) program as one of SBA's Top Ten Most Critical Management Challenges for the last eight years citing several problems – most recently including lack of staffing resources – that deserve attention but which remain unresolved. Additionally, a number of the participants are Alaska Native Corporations that are receiving a substantial portion of the available contracts. The Government Accountability Office has been reviewing issues with the growth of Alaska Native Corporations that make up less than 2 percent of all 8(a) firms but have been awarded over 20 percent of all 8(a) contract dollars – a tenfold increase since FY 2000.

The current funding level is insufficient to manage the growth of the 8(a) program, supporting the participants adequately, and addressing critical problems such as oversight and contract award. SBA's FY2009 budget proposal – a mere 5 percent increase from the FY 2008 request – does nothing to address the established problems and does not assign resources commensurate with resolving the pervasive management challenges raised by the GAO and the IG. The Committee would like to see the program supported at a level that allows for assistance to more 8(a) firms from headquarters and in the field offices and sufficient oversight to ensure the program is managed fairly and efficiently.

The 7(j) Program – This initiative provides management and technical assistance to 8(a) program participants and other businesses owned by socially or economically disadvantaged individuals. Section 7(j) of the Small Business Act authorizes grants to provide for such assistance. The 7(j) program is the primary way 8(a) program participants receive technical assistance from the SBA. While the Administration's policies have dramatically increased the pool of 8(a) participants, they propose $1.53 million, a 24 percent decrease in funding for 7(j) from the FY 2008 request. Reducing the program's budget request at a time of dramatic 8(a) growth puts the agency in the position of leveraging its resources to the point of ineffectiveness. The technical assistance has simply failed to keep pace with the growth. The Committee recommends providing the SBA with sufficient resources to support a grant budget of $5 million.

A review of 7(j) awards from 2000 through 2007 has disclosed a concerning trend that the agency is reducing the amount of grants provided, thereby consolidating funding to one or two assistance providers per year. Most recently, a probe by the Committee found that one of the two awards in FY 2007 – accounting for more than 90 percent of that year's funds – was made to a company with not only little experience in management training, but with strong political ties to the current Administration. At the Committee's prompting, this case is currently under investigation by the agency's Inspector General's office. This situation raises concerns not only about the internal controls involved in the awarding of 7(j) funds, but also the 8(a) program approval process. Thus, the Committee strongly opposes the Administration's request to combine 7(j) funds with the agency's salaries and expenses account which would reduce transparency at a time when just the opposite should be occurring.

The HUBZone Program – The HUBZone program was established to expand community development for low-income or high unemployment areas through the injection of federal contracting dollars to businesses that locate in these areas and employ area residents. Despite an average cost to run the program of $9 million per year, the Administration provides a line item of only $2 million in FY 2009. The FY 2008 request, while slightly above the 2007 request is less than 25 percent of the program's actual cost to taxpayers.

The Committee continues to have concerns that the SBA's on-going lack of commitment to the program in the form of insufficient resources devoted to its operations exacerbates the program's vulnerability to fraud, waste and mismanagement. The agency continues to downplay these risks as evidenced by their goal of performing an Internet-based review of five percent of program participants each year. This is particularly concerning in the face of overwhelming evidence from two reports by the agency's own Inspector General that the program continues to be subject to contracting fraud. The agency's on-going lack of support virtually ensures that communities in need of assistance will continue to be denied, with program benefits accruing to more affluent areas. Further, the Committee strongly opposes the Administration's request to blend HUBZone program funding requests with the agency's salaries and expenses account. If the existing budget transparency is removed, the agency's spending priorities for this program will be unnecessarily obfuscated.

The Women's Procurement Program – This initiative was created over seven years ago with the enactment of P.L. 106-554. From that time to the present, there is still no initiative that will allow women to compete against each other for contracts in industries that have historically been closed to them. The SBA is currently accepting comments on its second proposed rule to implement the program.

In its FY 2009 budget, the SBA requested no funding for the implementation of this program. This will nearly ensure that the program will not be available to women entrepreneurs in FY 2009. The result will be the fifteenth consecutive year that the women's procurement goal of five percent will not be met, costing women entrepreneurs tens of billions of dollars in lost contracting opportunities. In this time of economic uncertainty women business owners need the leveling of the playing field that the procurement program would provide now more than ever. Given this, the SBA's lack of support for this initiative in the form of resources to provide training to other agencies, staffing support to review cases of misrepresentation, and outreach to women entrepreneurs is particularly concerning to the Committee.

Procurement Center Representatives (PCRs) – The SBA's PCRs have historically provided assistance to aspiring small business federal contractors and challenges to one of the biggest obstacles small businesses face in the federal marketplace: contract bundling. Bundling combines small contracts that entrepreneurs could perform into giant packages that are beyond the capabilities and capacity of small firms. The SBA's PCRs are charged with reviewing bundled contracts in order to expand contracting opportunities for small businesses. If PCRs do not agree with an agency's bundling strategy, they can appeal the contract to the agency head. In its budget request, the SBA intends to raise the PCR staffing ceiling to 60. A 2005 SBA Inspector General's report IG cited staffing concerns.

In July of last year, the SBA began a new effort towards making greater use of its current complement of PCRs. The agency intends that PCRs focus solely on working with federal agencies and no longer interface with small businesses but instead referring them to SBA's "resource partners." In the 2005 IG report referenced above, the SBA noted in response to the IG's recommendations that "if bundling is real, a small business should come forward to notify SBA..." The Small Business Act empowers only the Administrator and the PCRs to intervene on behalf of small businesses in matters of bundled contracts. As a result, the SBA's attempt to leverage its PCR resources in this manner leaves small businesses that are affected by contract bundling with no advocate who has the ability to intervene in or affect the outcome of a contract bundling problem.

Therefore, the Committee supports more resources to PCR, especially given the more than doubling of federal contract dollars in the last decade and a staggering increase in federal contract bundling. The Administration itself has emphasizes the pivotal role PCRs play in monitoring bundling. The Committee believes the agency should have at least 75 PCRs, which the Committee recommended in its last authorization bill. The Committee also believes that sufficient travel money must be made available so each PCR can keep up with contracts they may need to monitor outside their local area.

Commercial Marketing Representatives (CMRs) – CMRs help small businesses become subcontractors to large corporations through research of available contracts and opportunities and advocacy and coordination with qualified small business candidates. The Committee recommends the SBA raise the number from its current level to 50 CMRs; one per state.

Office of Size Standards – This office carries out the SBA's authority to determine whether companies are "small businesses" for federal programs and regulations. Over the past few years, the Office of Size Standards has been so focused on revising various standards, that it has had trouble keeping up with agency and industry demands for determinations. However, the SBA's budget does not break out this office separately. The Committee recommends that the SBA list separately the resources of this office in their budget so that historical comparisons can be made for oversight purposes and that more resources can be specifically allocated to this function so they can do their job in a timely and effective manner.

ENTREPRENEURIAL DEVELOPMENT PROGRAMS

The FY 2009 SBA Budget proposes to reduce or flat fund virtually all of the entrepreneurial development programs. Due to the Administration's consistent resource cuts, SBA's entrepreneurial programs offer declining and less effective counseling even as they are expected to offset gaps created from contractions in the agency's other technical assistance programs.

In the Committee's view, the Administration's proposal impedes the agency from fulfilling one of its main objectives and the most critical for assisting US entrepreneurs gain the technical expertise associated with starting and operating a successful business. The fiscal plan will restrict entrepreneurial opportunities and drastically reduce the tools small businesses utilize for the initiation, investment, and expansion of their enterprises.

At a time of financial shortages and macroeconomic shocks, entrepreneurs are facing significantly challenging conditions. To adjust their enterprises and remain viable in the marketplace, entrepreneurs require access to affordable technical assistance resources. Through public investment in programs that help in the development of sustainable enterprises, small firms will continue contributing meaningfully to growing the nation's industries, sustaining communities, and generating productive, fulfilling employment.

SBA Emerging 200 Initiative – was proposed by the agency this year to address negative job growth experienced in several inner-city regions around the country. The pilot program will provide a single grant of $250,000 for a technical assistance provider to partner with 10 cities working to promote the growth of 200 inner city companies.

The agency's proposed initiative will exceed the cost of operating many of the individual existing entrepreneurial development facilities while servicing significantly fewer clients. Comparatively, sixteen states each received a total of $500,000 last year to operate multiple Small Business Development Centers with greater assistance levels. For example, at twice the cost of the new initiative, the state of Alaska operates six sub-centers through its SBDC program assisting over 2,500 clients each year. Further, the maximum grant for Women's Business Centers is $150,000 per year and many of these centers currently focus their training program on inner city entrepreneurs. The Committee is therefore concerned with the program design, particularly the minimal and duplicative impacts expected as a return for significant investment.

Given the initiative's proposed design, it is also not clear that the program goals will be achieved. The agency has failed to provide information on the program's type of technical assistance to be offered; qualifications for the selected trainer; or the approach for outreach to inner city businesses. Without certainty regarding the program's administration and outcomes, funding would be better appropriated to existing entrepreneurial development programs that have the regulations, processes, as well as local networks in place to support businesses in these communities.

The Administration's budget cuts, particularly targeting the agency's entrepreneurial development programs, are attributed to lack of adequate resources as well as the existence of a strong network of existing programs to address new needs. The Committee therefore recommends that the program resources are distributed to the core entrepreneurial development programs to more effectively fulfill this portion of their mandate.

Small Business Development Centers – was created by Congress through the Small Business Development Center (SBDC) program in 1980 to foster economic development by providing management, technical and research assistance to current and prospective small businesses. SBDCs offer one-stop assistance to small businesses by providing information and guidance in over 1000 central and easily accessible branch locations; generally in partnership with state and local educational communities. The Administration's FY 2009 budget proposes to cut 10 percent of the program resources from last year's funding level, which is roughly $37 million below their authorized level. Like other entrepreneurial development programs, SBDCs have been flat-funded for years while given a host of new responsibilities by the Administration and Congress. The program saw an increase in appropriated amount to $97 million in FY 2008, up from $87 million which was the amount appropriated in every year since 2001. The SBA has proposed reducing the program back down to $87 million and suggested SBDCs take over Microloan program counseling with no additional funding. This is similar to past requests to have the SBDCs take over BusinessLINC, FAST, Rural Outreach and Veteran outreach programs.

As with many other SBA programs, the Committee believes that the SBDC program should be increased. An appropriate budget level would be \$140 million. This funding level is critical to improve the program's service quality and supply, particularly as Americans seek new economic opportunities. The centers require additional resources to address problems arising with a high degree of urgency and complexity for small businesses, such as regulatory obstacles, health care choices, and disaster recovery procedures.

In response to many of these rising challenges, Congress required the agency to enhance the SBDC program, specifically by enacting new initiatives for energy efficiency assistance and to expand entrepreneurial opportunities for veterans. Thus far, the agency has failed to provide separate funding and institutional resources to implement these initiatives. The Committee recommends funding for these initiatives, but expects the core SBDC program to be fully funded before resources are directed to new services.

By cutting the overall program's budget, the agency is ceding its responsibility to provide entrepreneurial development assistance that has been mandated by Congress. Centers are expending increasing amounts of program time identifying new investment opportunities just to maintain operations rather than delivering vital services. Reduced support for the centers will further exacerbate struggles currently experienced in communities as they adjust to macroeconomic shocks, such as rising oil costs, and declines in local industries.

Women's Business Centers – provide assistance and/or training in finance, management, marketing, procurement and the Internet, and address specialized topics such as home based businesses, corporate executive downsizing, and welfare to work. All of the 96 centers provide individual business counseling and access to the SBA's programs and services – a number are also intermediaries for the SBA's Microloan and loan pre-qualification programs. The Administration's FY 2009 budget proposal cuts the program's funding since last year by nearly 10 percent. Due to funding limits, no new centers are projected to be created in the upcoming year and existing centers will face continued budget cuts.

The Committee recommends that \$17 million is provided for the WBC program to ensure funding for existing centers as well as those proposed to be initiated, particularly in socio-economically disadvantaged communities. For the agency to fulfill its mandate to serve one of the fastest growing and most successful small business sectors, these services must grow commensurate with future needs. As economic weakness afflicts local communities nationwide, particularly in underserved areas, it is critical that there are affordable, accessible tools for self-employment and productivity.

Service Corp of Retired Executives (SCORE) – trains start-up business owners through one-on-one counseling and workshops. Working and retired executives and business owners donate their time and expertise as volunteers, providing confidential counseling and mentoring free of charge. For FY 2009, the budget request is \$4.95 million, the same as the FY 2007 and 2008 requests. This is nearly \$2 million below the authorized level of \$7 million. Given the additional duties suggested fore SCORE and the amount of time that has passed since funding was increased, the Committee recommends funding SCORE at its fully authorized level of \$7 million.

Veterans Programs – the SBA relies on the Office of Veterans Business Development (OVBD) for overall veterans outreach. It is responsible for the formulation, execution, and promotion of policies and programs of the Administration that provides assistance to small business concerns owned and controlled by veterans and service-disabled veterans. It also currently administers six Veterans Business Outreach Centers (VBOCs), which are responsible for ensuring veterans access to capital through marketing and outreach efforts. The program was allocated $2 million for FY 2003 through 2006. The FY 2008 budget request asks for $743,000 for Veterans Outreach programs, the same as the FY 2008 request.

The level requested by the Administration for these services is under-funded and not on par with the rising needs of our veterans. With the call up of tens of thousands of National Guard and Reservists as well as the changing composition of this population, including 1/5th that are service disabled and 15 percent women, the agencies resources are currently below the capacity to meet these emerging needs. Further, one of the most critical aspects of entrepreneurial development – the hands-on counseling afforded through local training centers – is geographically limited through the minimal outreach centers.

To address these gaps in services, Congress recently enacted legislation increasing authorization levels for SBA's OVBD, as well as the number of VBOCs. Yet, the budget proposal fails to incorporate both the plans and the resources to implement the legislation. The Committee would like to see the commitment to returning veterans doubled both in resources allocated to the OVBD and in the $3 million allocated to expand the outreach and technical assistance efforts made to our veterans.

Paul Coverdell Drug Free Workplace Program – was created by the Drug Free Workplace Act (1998) which established a Drug Free Workplace Demonstration Program. The program, which provides grants to intermediaries and SBDCs to assist small businesses financially and technically in establishing drug free workplace programs, has not demonstrated any meaningful returns on the public investment. Since the entire federal government is experiencing severe budget contractions, the Committee cannot justify funding for a program that fails to produce measurable benefits.

National Women's Business Council – supports new and ongoing research and produces and distributes annual reports and recommendations prepared by the council. The President's FY 2009 budget request is $743,000 – the same as the FY 2008 request. The Committee recommends $750,000.

Office of Native American Affairs – ensures that American Indians, Native Alaskans and Native Hawaiians have access to business development and expansion tools available through the Agency's entrepreneurial development, lending, and procurement programs. In each of the last four years, no funds have been requested for the Office of Native American Affairs, but Congress and this Committee has continually funded the program. The FY 2009 budget request includes $1.6 million for the Office of Native American Affairs, although it is not a separate line item and, therefore, will not necessarily be distributed for appropriate program activities.

Adequate federal resources are particularly critical for the generally underserved communities in which this population lives. There are over 200,000 entrepreneurs of Native American heritage, and many continue to lack affordable access to the tools needed to start or expand enterprises. Through outreach and training, new opportunities will support self employment to stabilize household and regional economies.

Office of International Trade – was established to provide financing and technical assistance for small exporters facing obstacles accessing global markets. The Administration has targeted significant resource reductions for the agency's international trade program. Although last year, the agency requested an increase of 4 percent in funding, the program's budget has been reduced by nearly 22 percent since 2001. This has resulted in a nearly 30 percent decline in small business trade finance specialists located at US Export Assistance Centers, with no staff budgeted for the major port cities of New York City and New Orleans. Last year, the agency also financed 45 fewer international loans with a 10 percent decline in their value.

The Committee recommends that the Office of International Trade be allocated $3.1 million in order to return services back to its level at the beginning of the Administration's tenure. It is also recommended that Congress create a specific line item for this program as the agency has folded it into the operating budget, which decreases the transparency in which funds are used. With an enhanced trade promotion program at the agency, small exporters will be more competitive with their counterparts receiving export subsidies. Further, as the domestic economy continues to waver, small firms can pursue foreign consumers to stabilize and expand their marketshare.

OFFICE OF ADVOCACY

Advocacy was established by Congress to provide an independent voice for small business in the formation of public policy across the entire federal government. Advocacy also has funds available for independent, external research that focuses on small business trends, characteristics, and contributions to the economy. The Committee has long been concerned that there is a risk that Advocacy will lose its independence if its finances are controlled too closely by SBA.

In the FY 2009 budget submission, Advocacy's salary, benefits and operating expenses are folded into the SBA's Salaries and Expenses accounts under "Executive Direction." To date SBA has not interfered in Advocacy's employment level and has consistently funded approximately 48 positions within Advocacy for the last few years; but it is a concern. Also, Advocacy has some protection because the authority for the salaries and the duties of Advocacy are spelled out quite clearly in the Small Business Act independent of SBA's authority. However, this Committee has strongly supported a separate line-item for independent, extramural research for Advocacy that has been flat-funded at $1.1 million for some time. Congress created this line-item account a decade ago to further shield the independent judgment of this special function from SBA's direct or indirect influence. Advocacy, in its role as regulatory watchdog for small business under the Regulatory Flexibility Act, must render critical assessments of executive agencies from time-to-time, including the SBA; as well as collecting and analyzing data about small businesses and the impact of government regulations on them. Requiring Advocacy to look to SBA to dispense research funds chills their judgment in undertaking projects where the results, though valuable to small business, might run afoul of the Administration. The Committee strongly supports restoring the $1.1 million line-item for Advocacy Research and a separate report on funds requested for research in SBA's overall budget request.

ADMINISTRATION AND PERSONNEL OVERVIEW

In the FY 2008 budget presentation for this year, the SBA placed heavy emphasis on sizable increases in expenditures for training SBA employees. This is aimed a turning around serious prolonged problems with the morale and competence of its workforce. The SBA has lost about a third of its core workers over the last seven years, many to "incentive" driven buyouts, early retirement bonuses and directed relocations. It is estimated another third left and were replaced with lower grade and less experienced employees.

In addition, the SBA has now acknowledged that still another third are eligible for retirement before the end of FY 2009 - presenting another extraordinary management challenge, particularly in the field offices. All this might not matter if the federal activity with small businesses had diminished in the same period, but the opposite is true. Loan guarantee and financial package applications, technical assistance assignments, the volume of federal small business contract actions and the resources necessary for adequate oversight have all increased exponentially. Yet, personnel resources do not seem to reflect these needs.

There are ample indicators to support this concern. SBA ranked last in employee morale in the most recent Office of Personnel Management (OPM) Human Capital Survey (2006) and it had been near the bottom in the two previous polls. In addition, SBA ranked near the bottom in a customer satisfaction poll conducted by the University of Michigan, which could indicate that SBA does not have enough manpower to help small business owners when help is needed.

The Administration's budget request adds no new employees to fill critical needs beyond the 24 employees that would fill currently authorized slots. While the agency now recognizes it has a significant problem, the Committee is concerned that simply fulfilling its hiring obligation and adding to the training package is not enough. The Committee would like to see additional resources put back in place so that the agency can reconnect to the communities they serve. The current strategy does not benefit small businesses; particularly during times such as now when the economy is in decline.

CONCLUSION

With GDP growth at it lowest level since 2002 and the unemployment at its highest rate since 2005, the U.S. economy could use the economic contributions of small businesses. Small businesses create nearly 75 percent of net new jobs, often acting as the catalyst for the formation of new industries. The federal government has long had an interest in spurring entrepreneurship, doing so through the programs administered by the SBA. This most recent budget submission, however, diminishes the SBA's role significantly.

The Administration's FY 2009 budget submission does not take steps to make the SBA's access to capital programs more affordable and, as a result, these programs are unable to meet the credit needs of entrepreneurs during this challenging economic period. The Administration continues to shutter its largest venture capital program, the agency's sole seed capital initiative, and eliminates funding for the flagship 7(a) program. As a result, SBA will be unable to satisfy entrepreneurs' need for alternative forms of capital.

In its submission, the Administration also eliminates several programs critical to the economic development of low-income, urban, and rural communities. By terminating PRIME, SBIR FAST, SBIR Rural Outreach, and raising the cost of Microloans, aspiring small business owners will be left without the opportunities and resources to succeed. Making matters worse is that the Administration requests insufficient funding for the programs that will likely shoulder increased demand, including the Small Business Development Centers and the Women's Business Centers.

The Administration's FY 2009 budget submission for SBA represents the near culmination of the Administration's plan to dismantle the SBA. Without an adequate budget, SBA is left with no other alternative but to reduce its staffing levels, eliminate innovative initiatives and under fund other programs. If SBA's programs were fully funded and supported by the Administration, the agency would be able to spur the growth and the job creation that our economy needs.

Thank you for your consideration of the Committee's views on the Small Business Administration's FY 2009 budget submission.

With respect,

Nydia M. Velázquez

Nydia Velázquez
Chairwoman