

SBA'S 7(A) Lending Program

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Issue Update

Prior to April 2023, the Small Business Administration (SBA) capped at 14 the number of nondepository institutions licensed to make loans under SBA's Section 7(a) program. But in April, the SBA lifted the moratorium on that number, and in a separate rule also issued in April 2023, SBA amended various regulations governing the 7(a) program, including loosening underwriting standards for these loans.

Why It Matters

When SBA lifted the moratorium, it claimed it had the resources to supervise three new nonbank lenders. However, since then SBA has approved applications for an aggregate total of six new licenses without demonstrating it has the resources to supervise those new entrants to the 7(a) program, including four new licenses issued in December 2024. New fintech entrants are not subject to Federal prudential supervision. Therefore, they are not supervised to ensure compliance with BSA/AML laws, concentration caps, safety and soundness standards, and other regulations that promote prudent lending.

ABA is particularly concerned that SBA lifted the moratorium while simultaneously loosening lending standards for 7(a) loans. SBA replaced its long-standing nine-factor test with a requirement that lenders use credit analysis processes and procedures consistent with those used for their similarly-sized, non-SBA guaranteed, commercial loans. (By a subsequently issued procedural notice, SBA now requires more robust underwriting criteria for 7(a) loans greater than \$500,000—i.e., criteria that are similar, but not identical, to the nine-factor test that the 7(a) final rules removed.)

Recommended Action Items

To promote safe and sound 7(a) lending, ABA recommends that SBA:

- **Focus on increasing the number of highly regulated banks that participate in the 7(a) program instead of seeking new nonbank entrants to the program.** SBA should not grant any new SBLC licenses unless and until the agency demonstrates there is a small business lending "desert" that a new SBLC would serve and that SBA has the resources to oversee the new SBLC.
- **Resume publication of the franchise directory.** When SBA altered its rules regarding loans to franchises in April 2023, it discontinued the franchise directory, which had assisted 7(a) lenders with determining the eligibility of a franchisee for a 7(a) loan. The onus on checking affiliated business status now rests on the lender, increasing the cost of delivering capital to small businesses. SBA should continue to conduct eligibility reviews of franchisees and publish the franchise directory regularly.
- **Reinstate the Loan Authorization as a required document for 7(a) loans.** In the April 2023 final rule, SBA removed the Loan Authorization as a required document for 7(a) loans. The Loan Authorization had reflected SBA's commitment to guarantee the loan if specified conditions are met and removed any uncertainty about those conditions. This was particularly important if the lender who made the loan left the financial institution or if a party sought to make modifications to the loan after origination.
- **Require start-up companies seeking a 7(a) loan to provide a minimum injection of equity.** Prior to Jan. 2024, SBA required 7(a) borrowers to provide a 10% equity injection when the borrower is a startup (fewer than two years of business operations) or when the borrower is purchasing an existing business. This requirement better ensured the start-up company has the ability to repay the loan.