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SUMMARY

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Bruce R. Lindsay
Specialist in American National Government

Darryl E. Getter
Specialist in Financial Economics

Jared C. Nagel
Senior Research Librarian

Robert Jay Dilger
Senior Specialist in American National Government

SBA Disaster Loan Interest Rates: Overview and Policy Options

The Small Business Administration (SBA) is authorized to provide low-interest, long-term disaster loans, either on a direct basis or in partnership with private lenders, to eligible individuals, businesses, and nonprofit organizations to help them repair, rebuild, and recover from uninsured, underinsured, or otherwise uncompensated economic losses after a declared disaster. The SBA has relied exclusively on direct disaster loans since the early 1980s.

Congress provides appropriations for SBA disaster loan administrative expenses and disaster loan credit subsidies (the amount necessary to cover the program's non-administrative expenses). As a direct lending program, the SBA deposits disaster loan payments, including interest, into the SBA's Disaster Direct Loan Financing Account. These funds are then available for relending to other eligible disaster victims.

The SBA's disaster loan credit subsidy rate (the net present value of cash flows to and from the program, including loan payments, prepayments, interest subsidies, defaults, and recoveries) determines the amount of appropriations necessary to cover the program's non-administrative expenses. The loan credit subsidy rate is the program's non-administrative cost divided by the amount dispersed, which is expressed as a percentage of the amount dispersed. For example, in FY2020, the SBA disaster loan program's loan credit subsidy rate was 13.62%. This means that for each $1 appropriated for SBA disaster loan credit subsidies the SBA can provide about $7.34 in disaster loans.

The SBA disaster loan program's loan credit subsidy rate tends to be higher than other SBA loan programs because (1) its default rate tends to be higher than other SBA loan programs, (2) unlike most other SBA loan programs, the SBA is not authorized to charge disaster loan borrowers fees to help pay for expenses, and (3) disaster loan interest rates are determined by statutory formulas that underprice the risk associated with these loans. As a result, Congress provides appropriations for SBA disaster loan credit subsidies that otherwise could have been provided, at least in part, by borrower fees and higher interest rates.

The SBA's disaster loan interest rate formulas provide distinct limits for borrowers unable to secure credit elsewhere and for borrowers able to secure credit elsewhere. In recent years, some Members of Congress have argued that disaster loan interest rates should be lowered, or eliminated altogether, to provide greater relief for disaster victims. Some have also questioned whether SBA has the discretionary authority to lower disaster loan interest rates without legislative action. Others worry about the revenue that would be lost by doing so, and additional appropriations may have to be provided to keep the program whole. Some Members of Congress are reluctant to provide that additional funding, given the size of the federal government's debt and annual deficits.

This report opens with an overview of the SBA Disaster Loan Program's financing, followed by the history of SBA disaster loan interest rate policy and the statutory formulas that determine these rates. It also provides a more general overview of the SBA Disaster Loan Program and summarizes congressional debates over the extent to which the cost of these loans should be borne by borrowers or taxpayers. This report concludes with an assessment of various legislative options currently under consideration and the extent to which the SBA can administratively adjust disaster loan interest rates.

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Introduction

The Small Business Administration's (SBA's) Disaster Loan Program has been a major source of assistance for the restoration of commerce and households in areas stricken by natural and human-caused disasters since the agency's creation in 1953.[1] The SBA is authorized to provide disaster loans "either directly or in cooperation with banks and other lending institutions through agreements to participate on an immediate [shared] or deferred (guaranteed) basis."[2] Since the early 1980s, the SBA has exclusively offered direct, low-interest, long-term disaster loans to help eligible businesses, nonprofit organizations, and individuals and households to repair, rebuild, and recover from uninsured, underinsured, or otherwise uncompensated economic losses after a declared disaster.[3]

By law, the borrower's interest rate is determined by formulas, with distinct limits for borrowers unable to secure *credit elsewhere* (not to exceed 4%) and for borrowers able to secure credit elsewhere (not to exceed 8%).[4] In recent years, some Members of Congress have argued that these interest rates should be lowered, or eliminated altogether, to provide greater relief for disaster victims. Others worry about the cost of doing so, given the size of the federal government's debt and annual deficits.

Credit Elsewhere

The Small Business Act defines the term "credit elsewhere" for disaster loan purposes as "the availability of credit on reasonable terms and conditions from nonfederal sources taking into consideration the prevailing rates and terms in the community in or near where the applicant business concern transacts business, or the applicant homeowner resides, for similar purposes and periods of time."

15 U.S.C. §632(h)(2)

This report opens with an overview of the SBA Disaster Loan Program's financing, followed by the history of SBA disaster loan interest rate policy and the statutory formulas that determine these rates. It also provides an overview of the SBA Disaster Loan Program's four largest lending programs and congressional debates over the extent to which cost of these loans should be borne by borrowers or taxpayers. As will be discussed, the SBA is not authorized to charge fees to disaster loan borrowers; SBA's disaster loans are not underwritten to fully account for default risk; and the program's interest rates are determined by statutory formulas that generally require the SBA to charge below-market interest rates. As a result, the SBA Disaster Loan Program is purposively designed not to generate rates of return that fully cover the program's cost.

This report concludes with an assessment of various legislative options currently under consideration and the extent to which the SBA can administratively adjust disaster loan interest rates.

[1] See **Appendix C** for an explanation of why the U.S. Small Business Administration (SBA) administers the Disaster Loan Program instead of the Federal Emergency Management Agency (FEMA).

[2] 15 U.S.C. §636(b)(1)(A).

[3] In FY2019, the SBA approved about $2.44 billion in disaster loans. In FY2020, the SBA approved about $679 million in non-COVID-19-related disaster loans and $195.2 billion in COVID-19-related disaster loans. See SBA, *Agency Financial Report, Fiscal Year 2020*, p. 7, at https://www.sba.gov/document/report-agency-financial-report; and SBA, "Small Business Administration Loan Performance, Effective March 31, 2021: Table 2—Gross Approval Amount by Program," at https://www.sba.gov/document/report-small-business-administration-loan-program-performance.

[4] 15 U.S.C. §636(d)(5)(A)-(D) (interest rate caps); and 15 U.S.C. §632(h)(2) (credit elsewhere definition for disaster loan purposes).

SBA Disaster Loan Types

As aforementioned, the SBA's Disaster Loan Program currently provides direct loans to help businesses, nonprofit organizations, homeowners, and renters. Loans may cover the costs to repair or replace uninsured or underinsured property damaged or destroyed in a federally declared or certified disaster.[5] This program may also help small agricultural cooperatives recover from economic injury resulting from a disaster.

As described below, the SBA Disaster Loan Program has four major lending programs:

1. Real Property Disaster Loans for households;
2. Personal Property Disaster Loans for households;[6]
3. Physical Disaster Business Loans for businesses of all sizes, often called Business Physical Disaster loans; and
4. Economic Injury Disaster Loans (EIDLs) for small businesses and private nonprofit organizations.[7]

SBA Real and Personal Property Disaster Loans

SBA Real Property Disaster Loans and Personal Property Loans are available to eligible homeowners and renters who have incurred uninsured or underinsured damage to their home or personal property located in a declared disaster area.[8]

- **Real Property Disaster Loans** provide up to $200,000 to repair or restore the homeowner's primary residence to its pre-disaster condition.[9] The loans may not be used for home upgrades or additions, unless the upgrade or addition is required by city or county building codes. Secondary homes or vacation properties are ineligible.[10]
- **Personal Property Disaster Loans** provide homeowners and renters located in a declared disaster area with up to $40,000 to repair or replace personal property

[5] P.L. 83-163, the Small Business Act of 1953, as amended. P.L. 85-536, To Amend the Small Business Act of 1953, made the SBA a permanent agency and placed its disaster assistance programs in section 7(b) of the Small Business Act.

[6] Real Property Disaster loans for households and Personal Property Disaster loans for households are collectively called Home Disaster loans.

[7] See the SBA's regulations for Home Disaster Loans (13 C.F.R. §§123.100-123.108); Physical Disaster Business Loans (13 C.F.R. §§123.200-204); and Economic Injury Disaster Loans (13 C.F.R. §123.300-123.303). The SBA also provides Military Reservist Economic Injury Disaster Loans (see 13 C.F.R. §§123.500-123.513); and Immediate Disaster Loans (see 13 C.F.R. §§123.700-123.706). Prior to P.L. 116-123, the Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020, which made economic damage from the Coronavirus Disease 2019 (COVID-19) pandemic an eligible EIDL expense, most SBA disaster loans (approximately 80%) were awarded to individuals and households rather than to businesses.

[8] In certain circumstances individuals and households can use FEMA grant assistance and an SBA Home Disaster Loan to recover from a disaster provided they do not use the combined assistance for losses for which they have already been compensated or may expect to be compensated. For more information see CRS Report R45238, *FEMA and SBA Disaster Assistance for Individuals and Households: Application Processes, Determinations, and Appeals*, by Bruce R. Lindsay and Elizabeth M. Webster.

[9] 13 C.F.R. §123.105(2).

[10] 13 C.F.R. §123.105(2).

owned by the disaster survivor.[11] Eligible items include furniture, appliances, clothing, and automobiles damaged or destroyed in the disaster.

SBA Physical Disaster Business Loans

Almost any business regardless of size (other than an agricultural enterprise) or nonprofit entity whose real or tangible personal property is damaged in a declared disaster area is eligible for a Physical Disaster Business loan.[12] These loans are available to businesses to repair or replace uninsured or underinsured disaster-damaged property. Private nonprofit organizations such as charities, churches, and private universities are also eligible.

- **Physical Disaster Business loans** provide up to $2 million to repair or replace uninsured or underinsured disaster damages to physical property, including machinery, equipment, fixtures, inventory, and leasehold improvements.[13] Loan maturity is based on the applicant's ability to repay and is generally set at either 15 years or 30 years.[14] However, businesses with credit available elsewhere are restricted to a maximum term of seven years. Collateral is required for physical disaster business loans exceeding $25,000. The SBA will not decline a loan for lack of collateral, but requires the applicant to pledge collateral that the SBA has determined is available.[15]

SBA Economic Injury Disaster Loans

- **SBA Economic Injury Disaster Loans** (EIDLs) are available only to businesses located in a declared disaster area that have suffered *substantial economic injury*, are unable to obtain credit elsewhere, and are defined as small by SBA size regulations (which vary from industry to industry).[16] Small agricultural cooperatives and most private nonprofit organizations that have

Substantial Economic Injury

Pursuant to the Small Business Act, the term "substantial economic injury" means economic harm to a business concern that results in the inability of the business concern to:

- meet its obligations as they mature;
- pay its ordinary and necessary operating expenses; or
- market, produce, or provide a product or service ordinarily marketed, produced, or provided by the business concern.

15 U.S.C. §636(b)(3)(A)(iii)

[11] 13 C.F.R. §123.105(1).

[12] 13 C.F.R. §§123.200, 123.201(a). For a list of ineligible entities, see 13 C.F.R. §123.101 (e.g., if the owner has been convicted, during the past year, of a felony during and in connection with a riot or civil disorder or other declared disaster; the damaged property can be repaired or replaced with the proceeds of insurance, gifts, or other compensation).

An agricultural enterprise is a business "primarily engaged in the production of food and fiber, ranching and raising of livestock, aquaculture and all other farming and agriculture-related industries."

[13] 13 C.F.R. §123.202(a).

[14] SBA, Office of Disaster Assistance, "Disaster Assistance Program: Standard Operating Procedure," SOP 50 30 9, p. 109, at https://www.sba.gov/document/sop-50-30-9-disaster-assistance-program (hereinafter SBA, "Disaster Assistance Program: Standard Operating Procedure," SOP 50 30 9).

[15] SBA, "Disaster Assistance Program: Standard Operating Procedure," SOP 50 30 9, p. 12.

[16] For more information on size standards, see 13 C.F.R. §123.300 for eligibility requirements. Size standards vary according to a variety of factors, including industry type, average firm size, and start-up costs and entry barriers. Size

suffered substantial economic injury as the result of a declared disaster are also eligible.[17]

EIDLs provide up to $2 million to help meet financial obligations and operating expenses that could have been met had the disaster not occurred.[18] Loan proceeds can only be used for working capital necessary to enable the business or organization to alleviate the specific economic injury and to resume normal operations.[19] EIDL loan amounts are based on actual economic injury and financial needs, regardless of whether the business suffered any property damage.

The SBA Disaster Loan Program's Financing

All of the SBA's lending programs, disaster-focused and not, were originally funded through a revolving loan fund in the U.S. Treasury. In 1966, the SBA Disaster Loan Program was provided its own, separate revolving loan fund in the U.S. Treasury, which continues today.[20]

For funding purposes, the SBA requests advances from the Treasury's Disaster Loan Program account as needed, subject to the availability of funds. The SBA then manages these funds through the SBA's Disaster Loans Program Account, the Disaster Direct Loan Financing Account, and the Disaster Loan Fund Liquidating Account.

At the close of each fiscal year, the SBA pays the Treasury interest on the amount of advances outstanding at a rate determined by Treasury, "taking into consideration the current average market yield of outstanding marketable obligations of the Unites States having maturities comparable to the notes issued by the [SBA] Administration" to SBA disaster loan borrowers.[21] In this context, SBA notes refers to SBA disaster loans and the interest rate Treasury charges the SBA is what is referred to as the SBA's cost of money.[22]

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standards are codified at 13 C.F.R. Part 121. For further analysis, see CRS Report R40860, *Small Business Size Standards: A Historical Analysis of Contemporary Issues*, by Robert Jay Dilger. P.L. 116-123, the Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020, made economic injury related to the Coronavirus Disease 2019 (COVID-19) pandemic an eligible EIDL expense. As a result, EIDL loan volume increased dramatically. During FY2020, the SBA approved 3.6 million COVID-19-related EIDL loans totaling $194 billion, about 99% of all SBA disaster loans approved in FY2020.[16] In FY2019, the SBA approved $2.45 billion among all disaster loan programs. Agricultural enterprises are generally not eligible for SBA assistance so as to minimize duplication of services available at the U.S. Department of Agriculture. However, agricultural enterprises with 500 or fewer employees were temporarily made EIDL-eligible for damages related to COVID-19 (through December 31, 2021). See SBA, "Small Business Administration Loan Program Performance: Table 2—Gross Approval Amount by Program," effective as of March 31, 2021, at https://www.sba.gov/document/report-small-business-administration-loan-program-performance.

[17] 13 C.F.R. §123.300.

[18] U.S. Small Business Administration, *Economic Injury Disaster Loans*, https://www.sba.gov/funding-programs/disaster-assistance/economic-injury-disaster-loans.

[19] 13 C.F.R. §123.105(2).

[20] P.L. 89-409, An act to amend Section 4(c) of the Small Business Act, and for other purposes.

For the current month, fiscal year to date, and prior fiscal year to date outlays and receipts for the SBA's Disaster Loans Program account at Treasury, see U.S. Treasury, "Monthly Treasury Statement," at https://fiscal.treasury.gov/reports-statements/mts/.

[21] 15 U.S.C. §633(c)(5)(A). The SBA paid $7.6 billion in interest payments to the Treasury in FY2020. See U.S. Office of Management and Budget, "Appendix, Budget of the U.S. Government, Fiscal Year 2022, Small Business Administration," p. 1230, at https://www.whitehouse.gov/wp-content/uploads/2021/05/appendix_fy22.pdf.

[22] The cost of money (cost of funds) in government accounting is similar, but slightly different in meaning from its use in private sector banking and finance. Technically, federal agencies "borrow" from Treasury to fund loans, and their

The SBA also deposits disaster loan repayments (including interest received) into the revolving disaster loan fund to fund additional disaster loans. When loan demand exceeds the amount available in the disaster revolving fund, the SBA must request a supplemental appropriation to meet the demand, or risk violating the Anti-deficiency Act, which generally prohibits agencies from making or authorizing expenditures in excess of the amount available.[23]

Importantly for this discussion, the federal government's (and, therefore, the SBA's) cost of money is below the prevailing private sector market interest rate for loans of similar maturity and terms because Treasury securities are fully guaranteed by the federal government and are also exempt from federal taxation. As a result, the demand for Treasury securities is greater than the demand for private sector securities, resulting in lower interest rates for Treasury securities.

Charging disaster loan borrowers below-prevailing market interest rates (even if the interest rates are higher than the SBA's cost of money) can incentivize borrowing and further increase SBA's costs for administration (financed separately in appropriation acts) and costs related to loan defaults (which reduce the amount available to be redeposited into the disaster loan fund). As a result, when determining provisions governing SBA disaster loan interest rates, Congress takes into account and tries to balance the competing interests of borrowers and taxpayers. Setting interest rates lower than prevailing market interest rates benefits borrowers by reducing interest expense and the size of loan payments. However, the SBA (and by extension, federal taxpayers) incurs additional cost by doing so.

Also, although the SBA is authorized to charge borrowers fees in its non-disaster loan guarantee programs to help pay for program costs, including loan default costs, it is not authorized to charge disaster loan borrowers fees. As a result, debates about disaster loan interest rates involve judgments concerning (1) the extent to which these interest rates should meet the SBA's cost of money, (2) the extent to which these interest rates should fall below prevailing private sector market interest rates (which reflect private sector underwriting judgments related to the risk of nonpayment), and (3) the extent to which these interest rates should cover the SBA Disaster Loan Program's costs.

SBA Disaster Loan Interest Rate Policy: 1950s and 1960s

Initially, Congress did not include language in the Small Business Act concerning SBA disaster loan interest rates. The SBA set those rates administratively in 1953 at 3% for home disaster loans and 5% for business disaster loans.[24] By 1955, all SBA disaster loans had a 3% interest rate.[25] At

cost of funds is set equal to the risk-free rate. Then, loans to borrowers are priced as mark-ups above the risk-free rate following any restrictions placed by Congress. In contrast, when private lenders borrow funds to make loans, their cost of funds is below the risk-free rate, but their loans are still priced as mark-ups (also in the form of interest rate adjustments) above the risk-free rate to account for financial risks; otherwise they would simply purchase risk-free Treasury securities. For an example of loan pricing in the private sector, see CRS In Focus IF10993, *Consumer Credit Markets and Loan Pricing: The Basics*, by Darryl E. Getter.

[23] For additional information and analysis concerning the SBA Disaster Loan Account, see CRS Insight IN11433, *Supplemental Appropriations: SBA Disaster Loan Account*, by Bruce R. Lindsay, Robert Jay Dilger, and Jared C. Nagel.

[24] U.S. Congress, House Committee on Banking and Currency, *Extension of Small Business Act of 1953*, hearing on H.R. 4525, H.R. 5207, H.R. 5729, H.R. 6301, H.R. 7069, and S. 2127, 84th Cong., 1st sess., May 18, 1955 (Washington: GPO, 1955), p. 36.

[25] U.S. Congress, House Committee on Banking and Currency, *Extension of Small Business Act of 1953*, hearing on

that time, the SBA's Disaster Loan Program included both SBA direct disaster loans and loans issued through a SBA-private lender partnership, called participatory disaster loans. A participatory disaster loan was partially financed by the SBA (using SBA interest rates) and partially financed by a private lender (using interest rates set by the lender). SBA regulations specified that the private lender's interest rate on its share of the disaster loan had to be reasonable.

The first statutory provision directly affecting SBA disaster loan interest rates was enacted in 1955. P.L. 84-268 limited SBA disaster loan interest rates for the acquisition or construction of personal housing to no more than 3%.[26] The following year, P.L. 84-402 limited all SBA disaster loan interest rates to no more than 3%, which was the SBA's administratively-set interest rate in place at that time.[27] Advocates of the 3% limit argued that it was "sufficient to cover all Governmental costs in the program and possibly including an increment of profit."[28]

During the 1960s, with a few exceptions, the SBA administratively limited the interest rate charged by private lenders on their share of a participatory disaster loan for individuals to 3% (meaning interest for the entire loan was 3%) and to a reasonable interest rate for businesses.[29]

In 1969, the Nixon Administration, noting that the private sector's prime interest rate at that time had reached 8.5%, argued that the SBA's disaster loan interest rate cap caused the program to be "conducted at a very substantial loss to the Government" and recommended that the cap be replaced with a formula more aligned with prevailing market rates.[30] Later that same year, P.L. 91-79 retained the 3% interest rate cap for borrowers lacking access to credit from private sources (i.e., those who could not locate "credit elsewhere"), but increased the interest rate for borrowers with credit available from private sources to the cost of money ("at a rate equal to the average annual interest rate on all interest-bearing obligations of the United States having maturities of 20 years or more and forming a part of the public debt as computed at the end of the fiscal year next preceding the date of the loan, adjusted to the nearest one-eighth of one per centum").[31]

SBA Disaster Loan Interest Rate Policy: 1970s and 1980s

In 1973, P.L. 93-24 required the SBA to have the same disaster loan interest rates as the Farmers Home Administration (FmHA) as determined under the Consolidated Farm and Rural

H.R. 4525, H.R. 5207, H.R. 5729, H.R. 6301, H.R. 7069, and S. 2127, 84th Cong., 1st sess., May 18, 1955 (Washington: GPO, 1955), p. 36.

[26] P.L. 84-268, To Amend the Small Business Act of 1953.

[27] P.L. 84-402, To Amend the Small Business Act of 1953; 15 U.S.C. §636 (1956).

[28] U.S. Congress, House Committee on Banking and Currency, *Amendment to Small Business Act of 1953*, hearing on H.R. 7871, 84th Cong., 2nd sess., January 5, 1956 (Washington: GPO, 1956), p. 27.

[29] U.S. Congress, Senate Committee on Banking and Currency, Subcommittee on Small Business, *Additional Assistance for Disaster Victims*, hearing on S. 1796, 89th Cong., 1st sess., April 27, 1965 (Washington: GPO, 1965), p. 13.

[30] U.S. Congress, House Committee on Banking and Currency, Subcommittee on Small Business, *Small Business Legislation of 1969*, hearings on "several bills and a resolution relating to small business," 91st Cong., 1st sess., July 9, 1969 (Washington: GPO, 1969), p. 29.

[31] P.L. 91-79, the Disaster Relief Act of 1969, §7; and SBA, "Title 13—Business Credit and Assistance, Chapter 1—Small Business Administration (Revision 4), Part 120—Loan Policy," 35 *Federal Register* 16165-16166, October 15, 1970.

Development Act. This policy ensured that all federal disaster loans charged the same interest rate. As a result, SBA disaster loan interest rates were, temporarily, no longer determined by the Small Business Act.[32] At that time, the U.S. Department of Agriculture set FmHA disaster loan interest rates after taking into account the loan's purpose and the emergency's effect, capped at no more than 3%. As a result, prior to enactment, FmHA disaster loan interest rates were somewhat lower than SBA disaster loan interest rates. The act also increased FmHA's (and therefore the SBA's) disaster loan interest rate cap to 5%.

In 1975, P.L. 94-68 authorized FmHA to provide disaster loans for both actual losses sustained and other farmer needs, including on-going production costs. FmHA was authorized to charge varying disaster loan interest rates depending on the loan's purpose. The SBA was not provided these flexibilities. Instead, the SBA's disaster loan interest rates were capped at the average annual interest rate on all U.S. interest bearing obligations that form a part of the public debt (the cost of money), adjusted to the nearest one-eighth of 1% plus one-fourth of 1%.[33]

In 1976, Congress returned SBA's disaster loan interest rate determinations to the Small Business Act, primarily because the SBA and FmHA disaster loan interest rates were no longer linked statutorily.[34] P.L. 94-305 retained, in slightly modified form, the SBA's formula for setting its disaster loan interest rates in accordance with the cost of money:

> not to exceed the average annual interest rate on all interest-bearing obligations of the United States then forming a part of the public debt as computed at the end of the fiscal year next preceding the date of the loan and adjusted to the nearest one-eighth of 1 per centum plus one-quarter of 1 per centum. Provided, however, That the interest rate ... shall not exceed the rate of interest which is in effect at the time of the occurrence of the disaster.[35]

Subsequently, the Carter Administration strongly objected to legislative proposals to reduce disaster loan interest rates below the cost of money, arguing that such efforts would "encourage frivolous and unwarranted applications, exaggerated claims, and fraud."[36] In response to the Carter Administration's concerns that disaster interest rates were too low, in 1980, P.L. 96-302 modified the cost of money formula to allow the SBA to add up to an additional 1% (instead of one-quarter of 1%) to the calculated interest rate, but only if a borrower was able to obtain credit elsewhere.[37]

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[32] See P.L. 93-24, An act to Amend the Emergency Loan Program Under the Consolidated Farm and Rural Development Act, and for Other Purposes.

[33] See P.L. 94-68, A Bill to Amend the Consolidated Farm and Rural Development Act. Using the new formula, the SBA subsequently increased its disaster loan interest rate to 6.25% from 5%. See U.S. Congress, House Committee on Small Business, Subcommittee on SBA and SBIC Authority and General Small Business Problems, *Federal Natural Disaster Assistance Programs*, hearings, 95th Cong., 1st sess., April 6, 1977 (Washington: GPO, 1977), p. 23.

[34] U.S. Congress, House Committee on Small Business, *Amendments to Small Business Act and Small Business Investment Act*, report to accompany H.R. 9056, 94th Cong., 1st sess., September 26, 1975, H.Rept. 94-519 (Washington: GPO, 1975), pp. 6, 11.

[35] P.L. 94-305, An act to Amend the Small Business Act and Small Business Investment Act of 1958 to Provide Additional Assistance Under Such Acts, to Create a Pollution Control Financing Program for Small Business, and for Other Purposes; and 15 U.S.C. §636(b).

[36] U.S. Congress, House Committee on Small Business, Subcommittee on SBA and SBIC Authority and General Small Business Problems, *Federal Natural Disaster Assistance Programs*, hearings, 95th Cong., 1st sess., April 6, 1977, (Washington: GPO, 1977), p. 24.

[37] In addition, P.L. 96-302, To provide authorizations for the Small Business Administration, and for other purposes, required the SBA to determine, three years after disbursement, and every two years thereafter, if the borrower was able to obtain credit elsewhere at reasonable rates and terms. In that circumstance, the SBA was authorized to require the

The Reagan Administration went further than any other Administration, both before and since, in advocating for SBA program reductions (including a proposal that would have eliminated the SBA altogether).[38] For example, in 1981, the Reagan Administration, among many other changes, administratively restricted access to the Physical Disaster Business Loan program to businesses unable to obtain credit elsewhere. The Administration also reduced the loan amount available to eligible businesses from 100% to 60% of verified loss.[39] The Administration also recommended that agricultural enterprises lose their eligibility (which had been provided in 1976) to avoid duplication with FmHA,[40] end non-physical disaster loans entirely, and add a credit elsewhere test to limit SBA disaster loans to "only to those who cannot borrow from banks."[41]

In response, later that same year, Congress passed P.L. 97-35.[42] The act prevented the SBA from restricting Physical Disaster Business Loan eligibility to businesses that cannot obtain credit elsewhere and from limiting the loan to less than 100% of verified loss. However, in recognition of congressional support for the Reagan Administration's efforts to reduce SBA spending, the act also reduced disaster loan expenses, though not to the extent requested by the Administration and its congressional allies. To reduce costs, the act created new formulas for determining interest rates based on whether the applicant could obtain credit elsewhere. It also limited, but did not prohibit, SBA disaster loan access for businesses able to obtain credit elsewhere. Specifically, the disaster loan interest rate for homeowners unable to secure credit elsewhere was:

> the rate prescribed by the Administration but not more than one-half the rate determined by the Secretary of the Treasury taking into consideration the current average market yield on outstanding marketable obligations of the United States with remaining periods to maturity comparable to the average maturities of such loans plus an additional charge of not to exceed 1 per centum per annum as determined by the [SBA] Administrator, and adjusted to the nearest one-eighth of 1 per centum but not to exceed 8 per centum per annum.[43]

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borrower to accept such loan and repay the SBA disaster loan. At that time, eligible homeowners paid 3% on the first $55,000 of assistance and the cost of money (then 9.25%) above $55,000. Farmers (provided eligibility by P.L. 94-305 in 1976) were required to first seek assistance from the Farmers Home Administration, businesses unable to obtain credit elsewhere were charged 5% (up to $500,000 maximum) and businesses able to obtain credit elsewhere were charged interest at the cost of money (then 9.25%) (up to $500,000 maximum). See U.S. Congress, Senate Committee on the Budget, *Omnibus Reconciliation Act of 1981*, report to accompany S. 1377, 97th Cong., 1st sess., June 17, 1981, S.Rept. 97-139 (Washington: GPO, 1981), p. 948.

[38] U.S. Congress, Senate Committee on Small Business, S. 408, *A Bill to Authorize and Provide Program Levels for the Small Business Administration for Fiscal Years 1986, 1987, and 1988*, hearing on S. 408, 99th Cong., 1st sess., February 28, 1985, S.Hrg. 99-28 (Washington: GPO, 1985), pp. 214-296 (testimony of David Stockman, then-Director of the U.S. Office of Management and Budget).

[39] SBA, "Disaster Loans; Changes in Eligibility," 46 *Federal Register* 18526, March 25, 1981. EIDLs were not subject to the 60% of verified loss cap, but were limited to no more than $100,000.

[40] P.L. 99-272, The Consolidated Omnibus Budget Reconciliation Act of 1985 (Title XVIII—Small Business Programs), made agricultural enterprises ineligible for SBA disaster loans.

[41] U.S. Congress, House Committee on the Budget, Task Force on Enforcement, Credit, and Multiyear Budgeting, *Reagan Budget Changes in Federal Credit Programs*, hearing, 97th Cong., 1st sess., March 19, 1981 (Washington: GPO, 1981), p. 97.

[42] Judith Havemann, "Reagan Abandons Plan to Scuttle SBA," *Washington Post*, May 31, 1986. Available at https://www.washingtonpost.com/archive/business/1986/05/31/reagan-abandons-plan-to-scuttle-sba/948f098f-9c83-46f2-b185-0a05f91a0523/.

[43] P.L. 97-35, The Omnibus Budget Reconciliation Act of 1981 (Title XIX—Small Business, Small Business Budget Reconciliation and Loan Improvement Act of 1981).

The act determined the disaster loan interest rate for homeowners able to secure credit elsewhere in the same manner, except that it did not limit the rate.[44]

The disaster loan interest rate for businesses unable to obtain credit elsewhere was limited to no more than 8% annually. Businesses able to obtain credit elsewhere were charged:

> the rate prescribed by the Administration but not in excess of the rate prevailing in private market for similar loans and not more than the rate prescribed by the Administration as the maximum interest rate for deferred participation (guaranteed) loans under section 7(a) of this Act. Loans under this subparagraph shall be limited to a maximum term of three years.[45]

In 1984, P.L. 98-270 reduced the interest rate cap for homeowners unable to secure credit elsewhere from 8% to 4%, added an 8% interest rate cap for homeowners able to secure credit elsewhere, lowered the interest rate cap for businesses unable to obtain credit elsewhere from 8% to 4%, and replaced the interest rate cap for businesses able to obtain credit with the following:

> the rate prescribed by the Administration but not in excess of the lowest of (i) the rate prevailing in the private market for similar loans, (ii) the rate prescribed by the Administration as the maximum interest rate for deferred participation (guaranteed) loans under section 7(a) of this Act, or (iii) 8 per centum per annum. Loans under this subparagraph shall be limited to a maximum term of three years.[46]

The only additional change to the disaster loan interest rate formulas took place in 2011. P.L. 112-74 increased the disaster loan term for businesses able to obtain credit elsewhere from three years to seven years.[47]

Current SBA Disaster Loan Interest Rate Policy

The SBA's current statutory disaster loan interest rate formulas are provided in **Table 1**. In all cases, the SBA's disaster loan interest rates applied are those in effect on the date the disaster occurred.

Table 1. Current Statutory SBA Disaster Loan Interest Rate Formulas

By Entity

Individuals and Households	
Individuals and Households Unable to Secure Credit Elsewhere (SBA Home Disaster loans)	"the rate prescribed by the [SBA] Administration but not more than one-half the rate determined by the Secretary of the Treasury taking into consideration the current average market yield on outstanding marketable obligations of the United States with remaining periods to maturity comparable to the average maturities of such loan plus an additional charge of not to exceed 1 per centum per annum as determined by the Administrator, and adjusted to the nearest one-eighth of 1 per centum, but not to exceed 4 per centum per annum." **Statutory Citation:** 15 U.S.C. §636(d)(5)(A).

[44] P.L. 97-35, The Omnibus Budget Reconciliation Act of 1981 (Title XIX—Small Business, Small Business Budget Reconciliation and Loan Improvement Act of 1981).

[45] P.L. 97-35, The Omnibus Budget Reconciliation Act of 1981 (Title XIX—Small Business, Small Business Budget Reconciliation and Loan Improvement Act of 1981).

[46] P.L. 98-270, Omnibus Budget Reconciliation Act of 1983 (Title III—Committee on Small Business).

[47] P.L. 112-74, the Consolidated Appropriations Act, 2012.

Individuals and Households Able to Secure Credit Elsewhere (SBA Home Disaster loans)	"the rate prescribed by the [SBA] Administration but not more than the rate determined by the Secretary of the Treasury taking into consideration the current average market yield on outstanding marketable obligations of the United States with remaining periods to maturity comparable to the average maturities of such loan plus an additional charge of not to exceed 1 per centum per annum as determined by the Administrator, and adjusted to the nearest one-eighth of 1 per centum, but not to exceed 8 per centum per annum." **Statutory Citation:** 15 U.S.C. §636(d)(5)(B).
Businesses, Private Nonprofit Organizations, or Other Eligible Concerns	
Businesses, Private Nonprofit Organizations, or Other Eligible Concerns Unable to Obtain Credit Elsewhere (SBA Economic Injury Disaster loans and Physical Disaster Business loans)	"not to exceed 4 per centum per annum." **Statutory Citation:** 15 U.S.C. §636(d)(5)(C).
Businesses Able to Obtain Credit Elsewhere (SBA Physical Disaster Business loans)	"the rate prescribed by the [SBA] Administration but not in excess of the lowest of (i) the rate prevailing in the private market for similar loans, (ii) the rate prescribed by the Administration as the maximum interest rate for deferred participation (guaranteed) loans under subsection (a), or (iii) 8 per centum per annum. Loans under this subparagraph shall be limited to a maximum term of 7 years." **Statutory Citation:** 15 U.S.C. §636(d)(5)(D).

Source: Based on Congressional Research Service interpretation of 15 U.S.C.

SBA's Application of the Statutory Interest Rate Formulas

As mentioned, SBA's disaster loan interest rates are capped by statutory formulas, with separate limits for borrowers unable to secure credit elsewhere (not to exceed 4%) and for borrowers able to secure credit elsewhere (not to exceed 8%).

SBA Disaster Loan Interest Rate Limits

SBA disaster loans have statutorily-set interest rate ceilings, but no interest rate floors. If the statutory calculations yield an interest rate above the statutory ceiling, the interest rate defaults to the ceiling.

SBA Home Disaster loans: 8% per annum, or 4% per annum if the applicant is unable to obtain credit elsewhere.

SBA Physical Disaster Business loans: 8% per annum, or 4% per annum if the applicant is unable to obtain credit elsewhere.

SBA EIDL: 4% per annum.

15 U.S.C. §636(d)(5)(A)-(D)

To receive an SBA disaster loan, applicants must have a credit history acceptable to the SBA. Generally, the SBA reviews the applicant's credit reports to determine if obligations, including any current or past federal debts, have been or are being met.[48] Applicants must also show the ability to repay all loans. Generally, the SBA analyzes the applicant's federal tax returns and income information to substantiate repayment ability and uses that analysis to determine loan maturities and repayment terms.[49]

[48] SBA, "Disaster Assistance Program: Standard Operating Procedure," SOP 50 30 9, p. 11; and 13 C.F.R. §123.6.

[49] SBA, "Disaster Assistance Program: Standard Operating Procedure," SOP 50 30 9, p. 11; and 13 C.F.R. §123.105(c).

With few exceptions, all SBA disaster loans are repaid in equal monthly installment payments of principal and interest which fully amortize the loan amount and the interest accrued during the initial deferment period (the first payment due date is typically five months from the date of the note) within the loan term.[50]

The maximum loan term for SBA disaster loans is generally 30 years, and is based on the applicant's ability to repay the loan. The maximum loan term for businesses able to obtain credit elsewhere is seven years.[51]

SBA Disaster Loan Interest Rate Determinations

In accordance with law, the SBA's current practice is to set disaster loan interest rates in the following manner:[52]

For *individuals and households unable to secure credit elsewhere*, the lower of the following options:

- one-half of the interest rate for individuals and households that are able to secure credit elsewhere; or
- the 4% statutory cap.

For *individuals and households able to secure credit elsewhere*, the lowest of the following options:

- the rate prevailing in the private market for what would be deemed a comparable mortgage loan (calculated by the SBA's Chief Financial Officer);
- the rate prescribed by U.S. Treasuries of comparable maturity length plus a mark-up of 1%, then rounded to the nearest 0.125%; or
- the 8% statutory cap.

For *businesses unable to obtain credit elsewhere*, the lowest of the following options:

- one-half of the rate prevailing in the private market for what would be deemed a comparable business loan (calculated by SBA's Chief Financial Officer);
- the rate prescribed by SBA as the maximum interest rate for 7(a) guaranteed loans (calculated as the prevailing prime rate plus a mark-up of 2.75%); or
- the 4% statutory cap.

For *businesses able to obtain credit elsewhere* (Physical Disaster Business Loans only, EIDL is not available to these firms), the lowest of the following options:

- the rate prevailing in the private market for what would be deemed a comparable business loan (calculated by SBA's Chief Financial Officer);

[50] SBA, "Disaster Assistance Program: Standard Operating Procedure," SOP 50 30 9, p. 110; and 13 C.F.R. §123.105(c). The deferment period may be extended. For example, for physical loans, when the construction/major repair will take a protracted period, the borrower may be unable to make full payments until the project is substantially completed. For economic injury loans, a later due date may be appropriate when there are major damages involving lengthy repairs, the injury period extends more than five months into the future, or the borrowing business is seasonal in nature.

[51] SBA, "Disaster Assistance Program: Standard Operating Procedure," SOP 50 30 9, p. 109.

[52] SBA, Office of Disaster Assistance, telephone and email communication with the authors, March 17, 2021.

- the rate prescribed by SBA as the maximum interest rate for 7(a) guaranteed loans (calculated as the prevailing prime rate plus a mark-up of 2.75%); or
- the 8% statutory cap.

For *nonprofit organizations unable able to obtain credit elsewhere*, the lower of the following options:

- one-half of the interest rate for nonprofit organizations that are able to obtain credit elsewhere; or
- the 4% statutory cap.

For *nonprofit organizations able to obtain credit elsewhere*, the lowest of the following options:

- the rate prevailing in the private market for what would be deemed a similar business loan (calculated by SBA's Chief Financial Officer);
- the rate prescribed by U.S. Treasuries of comparable maturity length rounded to the nearest 0.125%, plus a mark-up of 0.250%; or
- the 8% statutory cap.

SBA Disaster Loan Interest Rate Pricing

As mentioned, from a policy perspective, some Members argue that the SBA's disaster loan interest rates should be lowered, or eliminated altogether, to help SBA disaster loan borrowers. Others are concerned about the costs of doing so, particularly given the size of the national debt and annual budget deficits. There have been no recent congressional efforts to increase disaster loan interest rates to the level necessary to cover all program costs, or to impose fees to help pay for those costs, which are covered through appropriations. **Table 2** provides SBA appropriations from FY2005-FY2022 for disaster assistance (including supplemental appropriations), business loan credit subsidies, and all other SBA programs.

The debate over SBA loan interest rates has been over what constitutes the proper balance between costs (to taxpayers) and benefits (to disaster victims). As will be discussed, from a market risk perspective, SBA disaster loan interest rates are underpriced given the potential for default-related losses (often referred to as the loan's financials). The question Congress may consider is "To what extent should the SBA's disaster loan programs' interest rates be underpriced?"

Table 2. Small Business Administration Appropriations, FY2005-FY2022

(appropriations and available funds; $ in millions)

Fiscal Year	Disaster Assistance	Disaster Assistance Supplemental	Business Loan Credit Subsidies	Other Programs	Total Appropriation	Total Spent
2022 request	$178.0	$0.0	$6.0	$811.5	$995.5	NA
2021	$168.1	$35,460.0	$297,145.0	$46,723.7	$379,496.7	$406,748.8 anticipated
2020	$177.1	$70,582.0	$687,439.0	$3,782.4	$761,980.5	$589,169.4
2019	$10.0	$0.0	$4.0	$701.4	$715.4	$1,253.0
2018	$0.0	$1,659.0	$3.4	$697.4	$2,359.8	$1,828.7

Fiscal Year	Disaster Assistance	Disaster Assistance Supplemental	Business Loan Credit Subsidies	Other Programs	Total Appropriation	Total Spent
2017	$186.0	$450.0	$4.3	$696.5	$1,336.8	$1,123.0
2016	$186.9	$0.0	$3.3	$680.8	$871.0	$1,058.1
2015	$186.9	$0.0	$47.5	$653.2	$887.6	$921.2
2014	$191.9	$0.0	$111.6	$625.4	$928.9	$951.2
2013	$111.2	$740.0	$319.7	$583.6	$1,754.5	$1,375.0
2012	$117.3	$0.0	$210.8	$590.7	$918.8	$1,039.3
2011	$45.4	$0.0	$82.8	$601.5	$729.7	$1,002.9
2010	$78.2	$0.0	$83.0	$1,625.3	$1,786.5	$966.7
2009	$0.0	$0.0	$8.5	$1,336.7	$1,345.2	$980.8
2008	$0.0	$1,052.8	$2.0	$579.9	$1,634.7	$928.2
2007	$114.9	$0.0	$1.3	$455.6	$571.8	$1,053.6
2006	$0.0	$1,700.0	$1.3	$532.1	$2,233.4	$2,308.0
2005	$111.8	$929.0	$1.4	$498.0	$1,540.2	$907.7

Sources: U.S. Small Business Administration (SBA), *Congressional Budget Justification* [FY2005-FY2022]; for FY2011-FY2022, the SBA's *Congressional Budget Justification* is available at https://www.sba.gov/document/report-congressional-budget-justification-annual-performance-report. P.L. 117-2, the American Rescue Plan Act of 2021.

Notes: The appropriation figures in this table have been adjusted to account for rescissions.

The Underpricing of SBA Disaster Loan Financial Risk

As mentioned, Congress appropriates funds to the SBA for loan administration and disaster loan credit subsidies (the amount necessary to cover the program's non-administrative expenses, including those related to loan defaults). The amount to be appropriated for disaster loan credit subsidies is determined by the program's credit subsidy rate, which is the program's non-administrative cost divided by the amount dispersed. The credit subsidy rate is expressed as a percentage of the amount dispersed.[53]

The SBA's Office of Financial Analysis and Modeling is responsible for ensuring that the computation of subsidy rates for the SBA's credit programs are in compliance with the Federal Credit Reform Act of 1990 (FCRA). As indicated on the office's website,

> The FCRA requires all credit agencies, including the SBA, to budget and account for the cost of credit programs by determining the net present value of cash flows to and from the Government over the life of the portfolio and expressing the net amount as a credit subsidy rate. The process to develop a subsidy rate is lengthy and complex, requiring unique data collection techniques and analysis efforts. SBA develops its subsidy rates by creating models that incorporate data on loan maturity, borrowers' interest rates, fees, grace periods,

[53] A positive subsidy rate indicates a cost to the government and a negative subsidy rate indicates a budgetary savings. See U.S. Congressional Budget Office, *Estimates of the Cost of Federal Credit Programs in 2022*, October 2021, p. 4, at https://www.cbo.gov/publication/57412.

interest subsidies, delinquencies, purchases or defaults, recoveries, prepayments, advances and borrower characteristics.[54]

For example, in FY2020, the SBA disaster loan program's loan credit subsidy rate was 13.62%.[55] This means that for each $1 appropriated for SBA disaster loan credit subsidies the SBA can provide about $7.34 in disaster loans.

The SBA Disaster Loan Program's credit subsidy rate tends to be higher than other SBA loan guarantee programs because

1. its default rate tends to be higher (e.g., in FY2020, the SBA Disaster Loan Program's default rate (10.35%) was more than double the default rate for the 7(a) loan guarantee program (4.75%), the 504/CDC loan guarantee program (4.11%), and the Small Business Investment Company (SBIC) program's debentures (4.57%)),
2. SBA disaster loans do not have fees, and
3. SBA disaster loan interest rates are subject to statutory caps.[56]

Figure 1 provides an illustration of the credit subsidy rates (taking into account fees and other cash flows) for SBA disaster loans, Microloans, SBIC debentures, 504/CDC loans, and 7(a) loans from FY2015-FY2020.

The interest rate caps imposed by the SBA's disaster loan interest rate formulas contribute to the SBA Disaster Loan Program's relatively high loan credit subsidy rate because these formulas require the SBA to charge at or below prevailing market interest rates for disaster loans that would otherwise be available from the private sector.

In other words, for eligible borrowers, SBA disaster loan pricing does not account for various financial and risk metrics (e.g., borrower income, existing debt obligations) that private lenders take into account. Consequently, from an economic perspective, SBA disaster loans are purposively underpriced for risk.

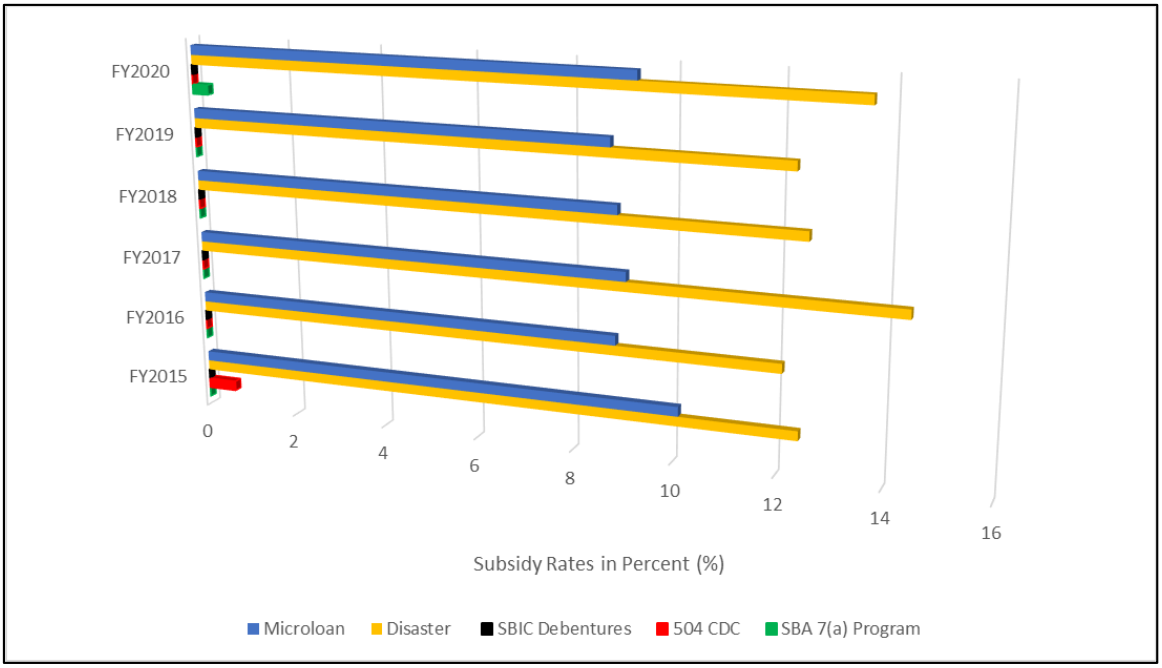
In finance, Treasury bond rates are referred to as *risk-free rates* because the federal government, unlike other borrowers, lacks certain financial risks such as default risk, the risk that a debt obligation will not be repaid on time or at all. Given that SBA disaster loans already carry interest rates at or below prevailing market levels for above-average levels of market risk, setting these rates equal to Treasury risk-free rates means that the SBA would receive no enhanced compensation for its willingness to assume enhanced levels of default risk.

[54] SBA, Office of Financial Analysis and Modeling, "Summary of Responsibilities," at https://www.sba.gov/about-sba/sba-locations/headquarters-offices/office-performance-management-chief-financial-officer/office-performance-planning-chief-financial-officer-resources#section-header-10.

[55] SBA, *Agency Financial Report, Fiscal Year 2020*, p. 84, at https://www.sba.gov/document/report-agency-financial-report.

[56] SBA, *Agency Financial Report, Fiscal Year 2020*, p. 84, at https://www.sba.gov/document/report-agency-financial-report. For additional information and analysis of the Small Business Investment Company program, see CRS Report R41456, *SBA Small Business Investment Company Program*, by Robert Jay Dilger.

Figure 1. SBA Total Credit Subsidy Rates for Selected Programs, FY2015-FY2020



Source: U.S. Small Business Administration, Agency Financial Reports, at https://www.sba.gov/document/report-agency-financial-report.

The SBA Disaster Loan Interest Rate Debate

Congress has debated the extent to which SBA disaster loan interest rates should generate revenue to help offset the program's costs since the program's inception. For example, in 1983, Senator Dale Bumpers stated the following at a congressional hearing concerning the use of credit elsewhere to set interest rates:

> How do you determine whether victims have credit elsewhere? I have mixed emotions about the credit elsewhere test. We debated that at length in the Senate when we passed that bill. I'm not interested in giving subsidized interest rates to very wealthy people and I don't think that ought to be the role of Government. That's one of the problems I've always had with student loans. The credit elsewhere test necessarily has to be very arbitrary.[57]

Many others testifying at that hearing, and several committee Members, argued that SBA disaster loan interest rates should be lowered to help people recover after a disaster.

Arguments For Lower SBA Disaster Loan Interest Rates

Historically, proponents of legislative efforts to lower SBA disaster loan interest rates have argued that, unlike typical SBA loan applicants (such as those seeking to start a new business), disaster victims, through no fault of their own, are already struggling to recover from unanticipated and adverse incidents. Requiring them to pay prevailing market interest rates, or even the somewhat lower than prevailing private sector market interest rates that often result from the SBA Disaster Loan Program's formulas, can create an additional burden for victims seeking

[57] U.S. Congress, Senate Committee on Small Business, *Disaster Loan Program*, hearing on the Disaster Loan Program, 98th Cong., 1st sess., March 29, 1983, S.Hrg. 98-101 (Washington: GPO, 1983), p. 49.

to recover and rebuild from a disaster. Furthermore, these proponents argue that the federal government should not make a profit on SBA disaster loans.

Table 3 provides a sampling of selected SBA disaster loan interest rates for various disaster declarations from 2015 to 2021.

Table 3. Selected SBA Disaster Loan Interest Rates, 2015-2021

Incident	Year	SBA Disaster Loan Interest Rates
COVID-19	2020 and 2021	**EIDL:** Small Business: **3.75%** Nonprofit: **2.75%**
Tropical Storm Imelda	2019	**Physical Disaster Loans:** Homeowners with Credit Available Elsewhere: **3.50%** Homeowners without Credit Available Elsewhere: **1.75%** Businesses with Credit Available Elsewhere: **8.00%** Businesses without Credit Available Elsewhere: **4.00%** Nonprofit Organizations: **2.75%** **EIDL:** Small Business: **4.00%** Nonprofit: **2.75%**
California Wildfires	2018	**Physical Disaster Loans:** Homeowners with Credit Available Elsewhere: **4.00%** Homeowners without Credit Available Elsewhere: **2.00%** Businesses with Credit Available Elsewhere: **7.48%** Businesses without Credit Available Elsewhere: **3.74%** Nonprofit Organizations: **2.75%** **EIDL:** Small Business: **3.74%** Nonprofit: **2.75%**
Hurricane Maria	2017	**Physical Disaster Loans:** Homeowners with Credit Available Elsewhere: **3.50%** Homeowners without Credit Available Elsewhere: **1.75%** Businesses with Credit Available Elsewhere: **6.61%** Businesses without Credit Available Elsewhere: **3.30%** Nonprofit Organizations: **2.50%** **EIDL:** Small Business: **3.30%** Nonprofit: **2.50%**
Hurricane Matthew	2016	**Physical Disaster Loans:** Homeowners with Credit Available Elsewhere: **3.12%** Homeowners without Credit Available Elsewhere: **1.56%** Businesses with Credit Available Elsewhere: **6.25%** Businesses without Credit Available Elsewhere: **4.00%** Nonprofit Organizations: **2.62%** **EIDL:** Small Business: **4.00%** Nonprofit: **2.62%**

Incident	Year	SBA Disaster Loan Interest Rates
Oklahoma Severe Storms, Tornadoes, Straight-line Winds, And Flooding	2015	**Physical Disaster Loans:** Homeowners with Credit Available Elsewhere: **3.37%** Homeowners without Credit Available Elsewhere: **1.68%** Businesses with Credit Available Elsewhere: **6.00%** Businesses without Credit Available Elsewhere: **4.00%** Nonprofit Organizations: **2.62%** **EIDL:** Small Business: **4.00%** Nonprofit: **2.62%**

Source: Compiled by CRS using data from the Federal Emergency Management Agency disaster declarations and U.S. Small Business Administration *Federal Register* notices.

Arguments Against Lower SBA Disaster Loan Interest Rates

Historically, opponents of legislative efforts to reduce SBA disaster loan interest rates, especially efforts to reduce those interest rates below the federal government's cost of money, to zero percent, or to convert the program into a grant program, worry that such actions could encourage borrowers to forgo or reduce their insurance coverage (called moral hazard, which occurs when individuals do not fully internalize the costs of their risk-taking).[58] They argue that lower interest rates could also lead to heightened demand, further increasing program costs. In their view, lowering disaster loan interest rates further, especially given that the program has no fees to help pay for program costs and a relatively high default rate, would be fiscally unwise.

In recent years, there have been no congressional efforts to charge SBA disaster loan borrowers prevailing private sector interest rates or to impose fees to move the program towards zero credit subsidy (self-financing).

An Administrative, as Opposed to Legislative, Response?

The SBA appears to have the statutory authority to charge disaster loan interest rates below the limits set forth by the formulas in P.L. 98-270, and, by selecting the lowest of the formulas' respective financial limiting factors, has done so, at least partially. The SBA could charge still lower interest rates. It could also, depending on the calculations for each the formulas' respective financial limiting factors, charge higher interest rates than it currently does. Apparently, the SBA has determined that its approach (using the lowest of the formulas' financial limiting factors to determine the disaster loan program's interest rates) is the appropriate balance between increasing cost to taxpayers and providing benefits to the borrower.

Concluding Observations

Throughout the years, Congress has expressed concern about the ability of businesses, nonprofit organizations, and individuals and households to recover from disasters. In an attempt to provide

[58] U.S. Congress, House Committee on Small Business, Subcommittee on Economic Growth, Tax and Capital Access, *Examining the Role of Government Assistance for Disaster Victims, A Review of* H.R. 3042, 112th Cong., 2nd sess., February 16, 2012, H.Rept. 112-55 (Washington: GPO, 2012), pp. 14-15. For additional information and analysis of the SBA Disaster Loan Account, see CRS Insight IN11433, *Supplemental Appropriations: SBA Disaster Loan Account*, coordinated by Bruce R. Lindsay. See also, RAND Corporation, *Insuring Public Buildings, Contents, Vehicles, and Equipment Against Disasters*, p. xvi, https://www.rand.org/pubs/research_reports/RRA332-1.html.

debt relief to disaster victims, several legislative proposals have been introduced in recent years to lower SBA disaster loan interest rates (see **Appendix B**). For example, S. 4167, the Small Business Disaster Loan Enhancement Act of 2020, introduced during the 116th Congress, would have established an interest rate of not more than 1% for any EIDL during the period beginning on February 15, 2020, and ending on December 31, 2020.

Measures similar to S. 4167 have also been introduced in recent years, but none have been enacted. Perhaps this is because a key tenet of current federal emergency management policy is that federal disaster assistance is seen as being supplemental in nature and not designed to make people and businesses whole again.[59] There is a general expectation that individuals, businesses and nonprofit organizations are responsible for taking necessary steps to protect themselves and their organizations from a disaster, including the purchase of adequate insurance coverage.[60] Although some may argue that the government's role is to help those in need by offering easily obtainable and subsidized disaster loans, others may argue that the SBA's disaster loans' terms are too favorable and might incentivize some to forgo or reduce insurance.

Congress has sought to negotiate the gap between the positions. For example, at a 2012 hearing entitled *Examining the Rode of Government Assistance for Disaster Victims: A review of* H.R. 3042, before the House Committee on Small Business, Subcommittee on Economic Growth, Tax, and Capital Access, Representative Schrader inquired:

> Let us talk about the moral hazard issue. That is something I am concerned about and I think... what is the even proper role between SBA and flood insurance? I mean, SBA would be a super [form of] disaster assistance, when things go beyond the norm, and obviously our flood insurance programs are not doing what they should be doing and... are worried about our debt and deficit at the federal level and so we are very conscious about the cost of this particular piece of legislation potentially. So what is the balance.... What is the role of the SBA versus flood insurance? What specific mitigation changes do we need to make in either program in your opinion to be more effective? And what is the magic interest rate that gets the right point to avoid moral hazard?[61]

Reaching a consensus on an appropriate disaster loan interest rate has thus far been elusive. In response to the inquiry, Howard Kunreuther, Professor of Decision Sciences and Public Policy at the Wharton School, University of Pennsylvania summarized the interest rate conundrum faced by Congress that continues to this day:

> That is a value judgment. It is a judgment that everyone has to make as to how much assistance we want to give and whether or not that money could have been spent better in other ways. I will not answer that question directly because I think at the end of the day we as a society, and Congress plays that role, has to judge at what point do we want to provide special relief. And it certainly could be argued that if it turns out someone would not be able to stay in business unless they were able to get a very, very small loan, a low interest loan, then you may want to go in that direction.[62]

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[59] FEMA, *A Citizen's Guide to Disaster Assistance*, "Unit Three: Overview of Federal Disaster Assistance," p. 56, September 2003. Available at https://training.fema.gov/emiweb/downloads/is7complete.pdf.

[60] W.J. Wouter Botzen, Howard Kunreuther, and Erwann Michel-Kerjan, "Protecting Against Disaster Risks: Why Insurance and Prevention May Be Complements," *Journal of Risk and Uncertainty*, vol. 59, no. 5 (October 19, 2009), pp. 151-169.

[61] U.S. Congress, House Committee on Small Business, Subcommittee on Economic Growth, Tax and Capital Access, *Examining the Role of Government Assistance for Disaster Victims, A Review of* H.R. 3042, 112th Cong., 2nd sess., February 16, 2012, H.Rept. 112-55 (Washington: GPO, 2012), pp. 14-15.

[62] Ibid., p. 15.

Appendix A. Disaster Declarations

There are five ways in which the SBA Disaster Loan Program can be put into effect. These include two types of presidential declarations as authorized by the Robert T. Stafford Disaster Relief and Emergency Assistance Act (the Stafford Act)[63] and three types of SBA declarations.[64] While the type of declaration may determine what types of loans are made available, it has no bearing on loan terms or loan caps. The SBA Disaster Loan Program becomes available when

1. The President issues a major disaster declaration and authorizes both Individual Assistance (IA) and Public Assistance (PA) under the authority of the Stafford Act.[65] When the President issues such a declaration, SBA disaster loans become available to homeowners, renters, businesses of all sizes, and nonprofit organizations located within the disaster area. EIDLs may also be made for victims in contiguous counties or other political subdivisions.
2. The President makes a major disaster declaration that only provides the state with PA. In such a case, a private nonprofit entity located within the disaster area that provides noncritical services may be eligible for a physical disaster loan or EIDL.[66] It is important to note that Home Physical Disaster Loans and Personal Property Loans are not made available to renters and homeowners under this type of declaration. Additionally, Business Physical Disaster Loans, and EIDLs are generally not made available to businesses (unless they are a private nonprofit entity) if the declaration only provides PA.
3. The SBA Administrator issues a physical disaster declaration in response to a gubernatorial request for assistance.[67] When the SBA Administrator issues this type of declaration, SBA disaster loans become available to eligible homeowners, renters, businesses of all sizes, and nonprofit organizations within the disaster area or contiguous counties and other political subdivisions.

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[63] For more information about Stafford Act declarations, see CRS Report R43784, *FEMA's Disaster Declaration Process: A Primer*, by Bruce R. Lindsay For an overview of FEMA disaster assistance, see CRS Video WVB00386, *2021 Hurricane and Disaster Seasons: FEMA Disaster Assistance Overview and Policy Considerations: Part 1*, by Diane P. Horn et al.

[64] Disaster declarations are published in the *Federal Register*. A list of current disaster declarations can be found on the SBA website at https://www.sba.gov/content/current-disaster-declarations.

[65] Administered by FEMA, Individual Assistance (IA) includes various forms of help for families and individuals following a disaster event. IA authorized by the Stafford Act can include housing assistance, disaster unemployment assistance, crisis counseling, and other programs intended to address people's needs. Public Assistance (PA) provides various categories of assistance to state and local governments and nonprofit organizations. Principally, PA covers the repair or replacement of infrastructure (roads, bridges, public buildings, etc.), but it also includes debris removal and emergency protective measures, which cover additional costs incurred by local public safety groups through their actions in responding to the disaster. FEMA's PA program provides assistance only to public and nonprofit entities. For more information on FEMA's PA program, see CRS In Focus IF11529, *A Brief Overview of FEMA's Public Assistance Program*, by Erica A. Lee.

[66] In order to receive FEMA grant assistance, these entities must first have applied for an SBA disaster loan and must have been deemed ineligible or must have received the maximum amount of assistance from SBA before seeking grant assistance from FEMA.

[67] The criteria used to determine whether to issue a declaration include a minimum amount of uninsured physical damage to buildings, machinery, inventory, homes, and other property. Generally, this minimum is at least 25 homes or businesses (or some combination of the two) that have sustained uninsured losses of 40% or more in any county or other smaller political subdivision of a state or U.S. possession. See 13 C.F.R. §123.3(3)(ii) and 13 C.F.R. §123.3(3)(iii).

4. The SBA Administrator may make an EIDL declaration when SBA receives a certification from a state governor that at least five small businesses have suffered substantial economic injury as a result of a disaster. This declaration is offered only when other viable forms of financial assistance are unavailable. Small agricultural cooperatives and most private nonprofit organizations located within the disaster area or contiguous counties and other political subdivisions are eligible for SBA disaster loans when the SBA Administrator issues an EIDL declaration.
5. The SBA Administrator may issue a declaration for EIDL loans based on the determination of a natural disaster by the Secretary of Agriculture.[68] These loans are available to eligible small businesses, small agricultural cooperatives, and most private nonprofit organizations within the disaster area, or contiguous counties and other political subdivisions. Additionally, the SBA administrator may issue a declaration based on the determination of the Secretary of Commerce that a fishery resource disaster or commercial fishery failure has occurred.[69]

[68] 13 C.F.R. §123.3(4).

[69] 15 U.S.C. §632(k)(1).

Appendix B. Selected Proposed Legislation Related to SBA Disaster Loan Interest Rates, 112th-117th Congresses

Below are selected bills from the 112th to the 117th Congress (2011-date of this report) that include provisions that adjust interest rates for SBA disaster loans. These bills were found by searching Congress.gov using the search terms "interest rate," "SBA," and "disaster loan." The bills listed below serve as examples, and not an exhaustive list of legislation.

112th Congress

H.R. 6296—Disaster Loan Fairness Act of 2012

- Would have amended the Small Business Act to provide the interest rate to be charged by the Small Business Administration (SBA) for loans made to small businesses beginning on January 1, 2011, and ending four years after the date of enactment of this act in major disaster areas. Would have required such rate to be the lesser of 4% or one-half the prevailing rate for similar loans in the area for those unable to attain credit elsewhere, or three-fourths the prevailing rate for those able to attain credit elsewhere. Would have required the SBA Administrator to refund excess interest payments made by qualifying borrowers before the enactment of this act.

113th Congress

H.R. 2857—Disaster Loan Fairness Act of 2013

- Would have amended the Small Business Act to provide the interest rate to be charged by the Small Business Administration (SBA) for loans made to small businesses 30 days after the date of enactment of this act or later in major disaster areas. Would have required such rate to be the lesser of 4% or one-half the prevailing rate for similar loans in the area for those unable to attain credit elsewhere, or three-fourths the prevailing rate for those able to attain credit elsewhere.

116th Congress

S. 4167—Small Business Disaster Loan Enhancement Act of 2020

- Would have authorized and provided funding for additional disaster loans and grants made to small businesses by the Small Business Administration (SBA) and temporarily limits the interest rate for certain economic injury disaster loans.

H.R. 6344—Expediting the EIDL Program Act of 2020

- Would have established a maximum interest rate on a disaster loan based on an applicant's ability to obtain credit elsewhere, and expanded the qualifying events for which a disaster loan may be awarded to include emergencies involving federal primary responsibility.

H.R. 6324—Too Small to Fail Act

- Would have required the SBA to waive the requirement that small businesses affected by the COVID-19 pandemic be unable to find credit elsewhere in order to be eligible for SBA loans, and required the SBA to provide loans made in response to the COVID-19 pandemic at no interest rate. In addition, would have authorized the SBA to temporarily defer payments on any SBA loan for a small business that is affected by the COVID-19 pandemic.

H.R. 6396—Responsible Relief for Americans Act

- Would have required the SBA to temporarily pay the principal, interest, and any associated fees that are owed on certain SBA loans.

117th Congress

H.R. 399—Border Business COVID–19 Rescue Act

- Would require the SBA to make loans of up to $500,000 to border businesses, with a zero percent interest rate. Would require loan recipients to use the funds to mitigate the effects of the COVID-19 pandemic on their business.

Appendix C. Why Does SBA Issue Disaster Loans Instead of FEMA?

In 1978, President Jimmy Carter signed Executive Order 12127. The order merged many of the disaster-related responsibilities of separate federal agencies into the Federal Emergency Management Agency (FEMA). During FEMA's formation, it was determined that SBA would continue to provide disaster loans through the Disaster Loan Program rather than transfer that function to FEMA. At the 1978 hearing before a Subcommittee of the Committee on Government Operations, Chairman Jack Brooks questioned the rationale for keeping the loan program outside of FEMA.[70] According to James T. McIntyre, Director, Office of Management and Budget (OMB), the rationale was as follows:

> [O]ne of the fundamental principles underlying this proposal is that whenever possible emergency responsibilities should be an extension of the regular missions of federal agencies. I believe the Congress also subscribed to this principle in considering disaster legislation in the past. The Disaster Relief Act of 1974 provides for the direction and coordination, in disaster situations, of agencies which have programs which can be applied to meeting disaster needs. It does not provide that the coordinating agency should exercise direct operational control.... [I]f the programs ... were incorporated in the new agency we would be required to create duplicate sets of skills and resources.... [S]ince the Small Business Administration administers loan programs other than those just for disaster victims, both the SBA and the new agency [FEMA] would have to maintain separate staffs of loan officers and portfolio managers if the disaster loan function were transferred to the new Agency.... [O]ne of our basic purposes for reorganization ... would be thwarted if we were to have to maintain a duplicate staff function in two or more agencies.[71]

McIntyre added, "We believe we have achieved a balance in this new agency [FEMA] between operational activities and planning and coordination functions." He further stated that "we can provide better service to the disaster victims if oversight of disaster response and recovery operations is vested in an agency which can adopt a much broader prospective than would be possible if this agency [FEMA] had operational responsibilities as well."

Additionally, the Stafford Act prohibits recipients of disaster aid from receiving similar types of aid from other federal sources and is often cited as a rationale for keeping the entities distinct. Section 312 of the act states

> The President, in consultation with the head of each Federal agency administering any program providing financial assistance to persons, business concerns, or other entities suffering losses as a result of a major disaster or emergency, shall assure that no such person, business concern, or other entity will receive such assistance with respect to any part of such loss as to which he has received financial assistance under any other program or from insurance or any other source.[72]

[70] U.S. Congress, House Committee on Government Operations, Subcommittee on Legislation and National Security, *Reorganization Plan No. 3 of 1978 (Federal Emergency Management Agency)*, hearing, 95th Cong., 2nd sess., June 26 and 29, 1978 (Washington: GPO, 1978), p. 13.

[71] Ibid.

[72] P.L. 93-288, 15 U.S.C. §5155(a).

Author Information

Bruce R. Lindsay
Specialist in American National Government

Jared C. Nagel
Senior Research Librarian

Darryl E. Getter
Specialist in Financial Economics

Robert Jay Dilger
Senior Specialist in American National Government

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