CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

May 1, 2007

S. 163
Small Business Disaster Response and Loan Improvements Act of 2007

As ordered reported by the Senate Committee on Small Business and Entrepreneurship on March 29, 2007

SUMMARY

S. 163 would amend the existing disaster loan program of the Small Business Administration (SBA), as well as authorize several new loan programs for small businesses. The bill would:

- Make economic injury loans available to nonprofit organizations;
- Increase the maximum loan that can be made for hazard mitigation purposes;
- Authorize SBA to contract with private entities to process loans and verify losses;
- Establish an immediate assistance program; and
- Guarantee certain private loans made to small businesses in response to a disaster.

Moreover, the bill would create two new direct loan programs for small businesses and agricultural producers suffering economic injury as a result of increased energy prices. CBO estimates that implementing S. 163 would cost $265 million over the 2008-2012 period, subject to the appropriation of the necessary funds. Enacting the bill would not affect direct spending or revenues.

S. 163 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of the bill is shown in the following table. The costs of this legislation fall within budget functions 350 (agriculture) and 450 (community and regional development).

	By Fiscal Year, In Millions of Dollars				
	2008	2009	2010	2011	2012
CHANGES IN SPENDING SUBJECT TO APPROPRIATION					
Disaster Loan Guarantees					
Estimated Authorization Level	34	35	35	37	38
Estimated Outlays	20	31	35	36	37
Energy Emergency Loans to Nonfarm Businesses					
Estimated Authorization Level	13	13	13	14	6
Estimated Outlays	8	12	13	13	10
Disaster Loans to Private Nonprofit Organizations					
Estimated Authorization Level	3	3	3	3	3
Estimated Outlays	2	3	3	3	3
Agricultural Producer Emergency Loans					
Estimated Authorization Level	3	3	3	3	0
Estimated Outlays	2	3	3	3	1
Other Provisions Affecting SBA					
Estimated Authorization Level	6	5	5	5	5
Estimated Outlays	4	5	5	5	5
Total Proposed Changes					
Estimated Authorization Level	59	59	59	62	52
Estimated Outlays	36	54	59	60	56

BASIS OF ESTIMATE

For this estimate, CBO assumes that the bill will be enacted before the end of fiscal year 2007, that the necessary amounts will be appropriated for each year, and that spending will follow historical patterns for current and similar programs.

The budgetary impact of the bill on SBA's credit programs is measured in terms of projected subsidy costs. Under the Federal Credit Reform Act, such subsidy costs are estimated and recorded on the budget on a present value basis. S. 163 does not specify an explicit loan level authorization for either the subsidy or the administrative costs for the amendments it would make to SBA's disaster loan program or for the new direct loan and loan guarantee programs authorized by the bill; CBO estimated those amounts using historical information about the demand for disaster loans and the past performance of SBA's disaster loan program.

Disaster Loan Guarantees

Section 202 would establish a new loan guarantee program for small businesses located in an area affected by a disaster. Under the proposal, a small business could apply directly to a qualified private lender for a disaster loan instead of applying to SBA, as under current law. The limit on individual loans would be $2 million and the federal government would guarantee up to 85 percent of the loan. In addition, the federal government would be authorized to pay a fee to the lenders for each loan originated under the program and to provide an interest rate subsidy of up to 3 percent.

CBO expects that demand for the new loan guarantee program would come from businesses that could otherwise obtain a loan from the private market. Assuming the maximum interest subsidy allowable under the bill, such borrowers would likely receive more favorable terms under the new loan guarantee program than currently offered by SBA or a private lender. (Businesses determined by SBA to be unable to obtain credit in the private market, however, would continue to receive more favorable terms under SBA's direct loan program and thus would not likely participate in the new guarantee program.)

CBO estimates that the federal government would guarantee about $100 million per year in loans under this new program. Included in this estimate is $50 million in loans to businesses that would otherwise borrow through SBA's direct loan program under current law. As such, the cost of those loan guarantees would be the marginal cost of subsidizing a loan guarantee rather than a direct SBA loan. In addition, our estimate includes about $50 million in loans to small businesses that would not have elected to obtain financing through SBA under current law. The additional cost for SBA to guarantee those loans, therefore, would equal the full subsidy cost of the new guarantees.

Assuming that SBA would guarantee 85 percent (the maximum guarantee level authorized) of these loans and would subsidize the interest rate at the maximum allowable level under the bill, CBO estimates that the subsidy rate for this new loan program would be 30 percent. As such, CBO estimates that implementing this new loan guarantee program would cost $20 million in 2008 and about $160 million over the 2008-2012 period for subsidy costs and administration.

Energy Emergency Loans to Nonfarm Businesses

Section 402 would authorize the SBA to provide loans up to $1.5 million to each small business that has suffered substantial economic injury as the result of increases in the price of heating fuel since October 2004. Small businesses could use loan proceeds to convert heating systems from heating fuel to renewable or alternative energy sources. Under the bill, the authority to make such loans would expire after four years.

The SBA disbursed an average of 1,300 Economic Injury Disaster Loans (EIDLs) per year over the 2003-2005 period (2006 was excluded due to abnormalities resulting from loans made to areas affected by Hurricanes Katrina, Rita, and Wilma), with each loan averaging about $75,000. CBO estimates that demand for the energy emergency loan program would increase the number of EIDLs by 40 percent. In addition, CBO expects that loans made to businesses with higher energy costs would be more risky than loans made under the regular disaster program. As such, CBO estimates that the subsidy rate associated with this program would be 20 percent (the estimated subsidy rate for the regular disaster program is 16 percent in 2008). Based on these parameters, CBO estimates that implementing this loan program would cost $8 million in 2008 and $56 million over the 2008-2012 for subsidy and administrative costs.

Disaster Loans to Private Nonprofit Organizations

Section 101 would expand SBA's EIDL program to include private, nonprofit organizations. Under current law, nonprofits may apply to SBA for physical damage disaster loans, but are not eligible to apply for economic injury loans. Based on the historical volume of physical disaster loans made to nonprofits and of EIDLs made to small businesses, CBO estimates that implementing this provision would cost $2 million in 2008 and $14 million over the 2008-2012 period for the subsidy costs of such loans and for administrative expenses.

Agricultural Producer Emergency Loans

Section 403 would amend an existing credit program administered by the Farm Service Agency of the USDA. The bill would expand eligibility for the emergency loan program to allow loans to producers with losses resulting from increased energy costs for the next four years. The Administration currently estimates that this program has a subsidy rate of 12 percent. In 2006, loan volume was $52 million. CBO estimates the proposed legislation would increase the volume of lending under the program by $25 million a year, with estimated subsidy outlays of $12 million over the 2008-2012 period.

Business Expedited Disaster Assistance Program

Section 204 would direct SBA to establish a short-term loan program for small businesses affected by a disaster. Loans made under this new program would be for less than 180 days and could be used to pay employees, make repairs, purchase inventory, or cover other necessary costs until such time that the business is able to obtain funding through insurance claims or other federal assistance. Such loans would carry an interest rate of up to one percent above the prime interest rate charged by a private lender and could be refinanced using any subsequent assistance provided by SBA. CBO expects that demand for other SBA loans would not be significantly diminished by this new authority, although additional risk would be incurred for borrowers that receive a short-term loan and are later denied a traditional disaster loan. SBA expects that because that situation is not likely to occur often, CBO estimates that this program would have a negligible cost over the next five years.

Disaster Mitigation Loans

Section 102 would authorize SBA to make or guarantee loans for disaster mitigation up to a maximum of 20 percent of the assessed damage to a home or business. Currently, SBA offers direct loans for disaster mitigation purposes purposes up to a maximum of 20 percent of an approved disaster loan. In some cases, SBA will make a disaster loan for less than the assessed damage due to factors such as reimbursements from other sources. Thus, S. 163 would increase the maximum amount of a disaster mitigation loan by 20 percent of the difference between assessed damages and the approved loan amount. The demand for such loans tends to be relatively small, and CBO estimates that implementing this provision would have a negligible effect on the federal budget over the next five years.

Contracting for Disaster Loan Processing and Verification

Section 111 would authorize SBA to enter into agreements with private contractors and lenders to process and verify losses for disaster loans during major or catastrophic disasters. For this work, SBA would pay a fee for each loan processed or loss verified. Assuming a minimal difference in the fee paid by SBA and the administrative expense that the government would otherwise incur, CBO estimates that implementing this provision would have a negligible effect on the federal budget.

Catastrophic National Disaster Loan Program

Section 201 would require the Department of Homeland Security, the Federal Emergency Management Agency, and SBA to establish a threshold for determining when an event would be deemed a catastrophic national disaster. Upon such a declaration, the SBA would be authorized under the bill to offer economic injury loans to small businesses nationwide that were adversely affected by the catastrophe. The terms of this loan program would be identical to the terms of the EIDL program under current law. SBA implemented a similar program following the terrorist attacks of September 2001. More than $500 million in economic injury loans were disbursed nationwide at a subsidy rate of abut 25 percent. Nonetheless, CBO cannot estimate the additional cost of this new loan program because CBO cannot predict the timing and severity of future disasters, nor what final criteria would be used to determine such an event. Over the next five years, we expect that the program would probably have a negligible cost because such disasters are rare.

Other Provisions Affecting SBA

Based on information from SBA, CBO estimates that implementing other provisions of S. 163 would require appropriations totaling $26 million over the next five years. That amount includes:

- $15 million to hire a full-time disaster planning specialist and other staff necessary to maintain the levels specified in the bill and to fulfill additional reporting requirements;

- $5 million to increase the maximum surety bond that SBA may guarantee for small businesses performing recovery work following a disaster who cannot obtain surety bonds in the private market;

- $5 million to establish a contracting outreach and technical assistance program for small businesses located in disaster areas; and

- $1 million to develop and execute simulation exercises to test the effectiveness of the disaster response plan.

Those estimates are based on information from SBA regarding costs of existing or similar programs. Based on historical spending patterns, CBO estimates that fully funding those activities would cost $4 million in 2008 and $24 million over the next five years, assuming appropriation of the necessary amounts.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

S. 163 contains no intergovernmental or private-sector mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

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