GAO Highlights

Highlights of GAO-20-618, a report to congressional committees

September 2020

SMALL BUSINESS LOANS

SBA Generally Incorporated Key Elements for Estimating Subsidy Cost of 7(a) Program

Why GAO Did This Study

The 7(a) program is SBA's largest loan guarantee program for small businesses, with about $95 billion in outstanding loan principal as of the end of fiscal year 2019. Federal agencies that provide credit assistance are generally required to estimate the net long-term cost to the government—known as the subsidy cost—for each annual cohort of loans. SBA initially estimated a zero subsidy cost for each cohort from fiscal years 2014 through 2019, but estimated that the fiscal year 2020 cohort would have a positive subsidy cost and require appropriations.

GAO was asked to evaluate SBA's subsidy estimation process for the 7(a) program. This report examines (1) how SBA estimates 7(a) subsidy costs, (2) the extent to which SBA incorporated key elements of subsidy cost estimation into its estimation process for the fiscal year 2020 budget, and (3) the changes SBA made in its estimation process for the fiscal year 2020 budget.

GAO reviewed SBA documentation on its estimation process, including information on SBA's cash flow model, and compared SBA's process to key elements that GAO previously identified (GAO-16-269). GAO also interviewed officials from SBA, the Office of Management and Budget, and outside auditors and contractors that annually review SBA's process and model.

View GAO-20-618. For more information, contact William B. Shear at (202) 512-8678 or shearw@gao.gov.

What GAO Found

The Small Business Administration (SBA) develops its subsidy cost estimates for the 7(a) loan guarantee program—that is, estimates of the program's net long-term cost to the government—using a cash flow model. The model uses historical data, econometric equations, and macroeconomic projections to estimate cash flows—such as guarantee fees, SBA purchases of defaulted loans, and recoveries on those loans—for the loans SBA expects to guarantee in the next fiscal year. The net present value of the cash flows (value in current dollars) is the subsidy cost estimate.

SBA generally incorporated key elements of subsidy cost estimation into its estimates for the 7(a) program for the fiscal year 2020 budget. Specifically, GAO found that SBA's estimation process was largely consistent with eight key elements GAO previously identified that help ensure subsidy estimates are supported, reliable, and reasonable. For example, SBA generally validated historical data, documented the cash flow model and key assumptions, analyzed the sensitivity of estimates to alternative assumptions, and had documented policies and procedures.

SBA made changes in its estimation process that collectively increased the 7(a) program's subsidy cost to $99 million for fiscal year 2020 (a 0.33 percent subsidy rate when expressed as the cost per dollar of credit assistance) from $0 for fiscal year 2019 (0 percent subsidy rate). Some of these changes were routine updates to data and economic assumptions used in the cash flow model, while others were revisions to the estimation process. Additionally, some individual changes increased the subsidy costs, while others decreased it. Some of the changes that had the largest impact on the subsidy rate included the following:

- Incorporating the President's economic assumptions for fiscal year 2020 decreased the rate by 0.27 percentage points.
- Updating the basis for the size and composition of the loan cohort SBA expected to guarantee in fiscal year 2020 increased the rate by 0.21 percentage points.
- Revising the methodology for estimating purchase amounts for defaulted loans to better reflect the outstanding loan balance at the time of purchase increased the rate by 0.21 percentage points.