



Audit Report



Report Number: OIG-SBLF-14-008

SMALL BUSINESS LENDING FUND:

Survey of Small Business Lending Fund Participants on
Use of Program Funds, Repayment Plans, and
Satisfaction with Treasury's Program Administration

March 27, 2014

Office of Inspector General

Department of the Treasury

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Abbreviations

CDLF	Community Development Loan Funds
OIG	Office of Inspector General
SBLF	Small Business Lending Fund
TARP	Troubled Asset Relief Program
The Act	Small Business Jobs Act of 2010

*The Department of the Treasury
Office of Inspector General*

March 27, 2014

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This is the second of two audit reports on the use of capital provided to financial institutions participating in the Small Business Lending Fund (SBLF). SBLF was created in December 2010 to provide capital to community banks with assets of less than \$10 billion. The funds came with incentives to stimulate small business lending. As of September 27, 2011, Treasury had invested \$4.03 billion in 332 institutions.

Our first report¹ addressed participant small business lending gains and progress in achieving qualified small business lending² plan projections. The audit objectives for this report were to: (1) determine how recipient institutions are using funds awarded under the SBLF program and the factors that most influenced their use of funds; (2) determine participants' plans to repay Treasury's investment and exit the program; and (3) evaluate Treasury's administration of the program.

¹ Report No. OIG-SBLF-13-012, *Small Business Lending Fund: Reported SBLF Program Accomplishments Are Misleading Without Additional Reporting* (August 29, 2013).

² Qualified small business lending is defined as business loans that are \$10 million or less, to businesses with \$50 million or less in annual revenue, for certain allowed purposes.

To accomplish our objectives we administered an email survey to 325 of 332 financial institutions participating in the SBLF program and analyzed their responses. The seven participants not surveyed were excluded because they had either merged with other banks or had requested not to participate. Of the 325 surveyed, 323 responded.

For the first objective, we asked participants to: identify how they used the SBLF funds; explain how the funds allowed them to increase small business lending, or, why they did not increase small business lending; estimate how much the funds increased their small business lending; and identify what factors influenced how they used the funds. We reported the estimates provided, although respondents may have used different methodologies in estimating how they used their SBLF funds. To accomplish our second objective, we asked participants about their plans to repay Treasury's investment. To accomplish our third objective, we asked participants if they were satisfied with Treasury's administration of the program. We then compared the responses for all three objectives by various sub-groups, such as the banks that received Treasury investments in the Troubled Asset Relief Program (TARP) and non-TARP banks.

We conducted our fieldwork from March 2013 to January 2014 in accordance with *Government Auditing Standards*. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained to address our audit objectives provides a reasonable basis for our findings and conclusions. Appendix 1 contains a more detailed description of our audit objectives, scope, and methodology.

Results in Brief

Almost all (94 percent) of the 323 survey respondents stated that as of the survey date they had used some or all of their SBLF

capital to extend credit to small businesses, and 6 percent said that all of the SBLF capital had been used for other purposes. However, 280 respondents, that collectively received approximately \$3.3 billion, could estimate how much of their SBLF funds supported small business lending. These respondents reported they used about \$1.8 billion (55 percent) for small business lending and \$1.5 billion (45 percent) for other purposes. The other purposes included paying dividends, redeeming equity or debt, increasing other types of lending, or holding non-leveraged capital, all uses that were allowed by Federal law.³

While most respondents indicated they used some of their capital for small business loans, 142 (52 percent) could quantify how much of the small business lending gains they reported to Treasury was attributable to the SBLF capital. These respondents estimated that \$1.4 billion (or 58 percent) of the \$2.4 billion they collectively reported as small business lending gains between the date of Treasury's investment and March 31, 2013, was a direct result of the SBLF funds.

While they did not estimate the amount of new lending that was attributable to SBLF funds, 98 percent of all survey respondents could identify the amount of new small business loans made since entering the program, and reported approximately \$22.8 billion in new small business lending. "New lending" differs from the lending gains reported by Treasury as they represent new loans and credit commitments. "Lending gains" reflect the difference in outstanding loan principal on a bank's books between two time periods, which can include loans made prior to the SBLF program and can be reduced by loan payoffs. The data we gathered showed that former TARP banks experienced similar small

³ As we noted in Report No. OIG-SBLF-13-012, *Small Business Lending Fund: Reported SBLF Program Accomplishments Are Misleading Without Additional Reporting* (August 2013), financial institutions cannot directly link SBLF capital provided by Treasury to loans or other uses. Financial institutions' reports of how they used their SBLF capital are based on subjective estimates, and the institutions' methodologies for making those estimates may vary.

business new lending activity relative to that of non-TARP banks, even though collectively they received less SBLF capital than the non-TARP banks. This could be due to a variety of factors, which the survey did not explore.

Treasury collects new lending information in its *Annual SBLF Lending Survey* of participants. However, Treasury did not clearly define new lending, and a significant number of participants incorrectly reported their new lending activity. Therefore, in order to more accurately report on new lending, Treasury will have to carefully define the term before administering its next *Annual SBLF Lending Survey*.

Eighty-two percent of the 323 respondents said that increasing small business credit demand was a factor in their decision to use their SBLF funds for small business loans. Additionally, sufficient loan profit margins and SBLF's incentive for lowering dividend rates were major factors driving their decisions to loan to small businesses. Respondents that reported using SBLF funds in ways that did not extend credit to small businesses said that a demand for other types of loans, margins on other types of loans, and the capital needs of their banks were the primary factors that influenced how they used their SBLF capital.

Our survey also disclosed that most respondents plan to repay Treasury's investment and exit the program when the variable dividend rate becomes fixed, or when cheaper capital is available. Finally, over 89 percent of respondents were satisfied overall with Treasury's administration of the SBLF program (excluding the handling of fees and penalties for non-compliance), especially with respect to the dividend rate-setting process, marketing materials, and amount of funds provided under the program. Fifty-two percent of the 98 respondents who rated their satisfaction with the process reported that they were unsatisfied with Treasury's handling of program fees and penalties.

We recommend that Treasury establish a clear definition of new

loans and commitments to small businesses before administering the next *Annual SBLF Lending Survey*. Treasury accepted the recommendation, but expressed concern with two findings. SBLF's Director said the report's statement that "52 percent of those who rated their satisfaction were unsatisfied with Treasury's handling of program fees and penalties" may mislead some readers. If the approximately 200 respondents who indicated that fees and penalties did not apply to them were included in the calculation of the satisfaction rate, only 51 of 321 respondents, or 16 percent, would be dissatisfied with fees and penalties, he said. Second, he expressed concern that survey respondents' estimates of how they used their SBLF capital are unreliable because funds cannot be directly linked to specific uses and respondents may have employed different estimation methodologies. A formal written response from Treasury is included in its entirety in Appendix 2.

Background

The Small Business Jobs Act of 2010 (the Act) created SBLF as a dedicated fund to encourage lending to small businesses by providing capital to qualified community banks⁴ and Community Development Loan Funds (CDLF). Treasury launched the SBLF program in December 2010 and by the program's September 27, 2011, funding deadline had disbursed \$4.03 billion. The funds were invested in 332 financial institutions, including 281 community banks and 51 CDLFs. Of the 281 community banks, 137 used SBLF funds to refinance securities purchased under TARP's Capital Purchase Program.

Treasury requires each SBLF participant to submit *Quarterly Supplemental Reports* indicating qualified small business lending gains. The Act defines qualified "small business lending" as business loans that are \$10 million or less to businesses with \$50 million or less in annual revenue.

⁴ The terms "banks" and "community banks" encompass banks, thrifts, and bank and thrift holding companies with consolidated assets of less than \$10 billion.

Treasury calculates small business lending gains as the difference between loans outstanding each quarter and the average amount outstanding in the four quarters ended June 30, 2010 (the baseline period).⁵ Banks adjust this calculation for charge-offs, loans guaranteed by the U.S. government, loans for which the risk is assumed by third parties, bank mergers, bank acquisitions, and purchases of loans.

At the time of our survey, June 2013, 15 institutions had fully redeemed their SBLF securities and exited the program, leaving 317 SBLF participants. As of December 31, 2013, 31 institutions had exited the program or merged with other participants, leaving 301 participants.

Most Respondents Used their SBLF Capital for Small Business Loans, but Only an Estimated 55 percent of the Awarded Funds Went to Small Business Loans

Almost all (94 percent) of the 323 survey respondents stated they used some or all of their SBLF capital to extend credit to small businesses. Most viewed the SBLF funds as a cheap source of capital to grow their small business lending programs and key to expanding their small business loan portfolios. The remaining 6 percent of respondents that collectively received \$185 million in SBLF funds did not extend credit to small businesses. The 6 percent included 15 former TARP banks and 4 non-TARP banks.

Of the 19 banks that reported that they had not extended credit to small businesses, most (10 respondents) did not provide an explanation. Of those respondents that provided an explanation, five reported they did not have adequate demand for small business loans, three reported that they had large pay-offs prior to

⁵ The Act defines the baseline period as “the 4 full quarters immediately preceding the date of enactment of this Act,” which comprises the quarters that ended September 30, 2009, through June 30, 2010.

SBLF funding that offset their lending increases, and one bank said the SBLF funds were used to exit TARP.

While most of the 323 respondents reported using a portion of their SBLF capital to extend credit to small businesses as the program intended, 280 (87 percent) were able to estimate how much of their SBLF capital was used for small business lending. We note that respondents may have employed different methodologies for estimating their uses of SBLF capital. As a result, the actual amounts used by category may vary from that reported below.

As shown in Table 1 below, the 280 respondents, who collectively received about \$3.3 billion (or 82 percent of the \$4.03 billion disbursed by Treasury), estimated they used \$1.8 billion (55 percent) of the SBLF funds awarded them to extend credit to small businesses. The remaining \$1.5 billion (45 percent) was used for purposes other than lending to small businesses.

Table 1: Respondents' Estimates of SBLF Fund Usage

Use of SBLF Funds	Number of Respondents	Funds Used	Aggregate Amount of Funding Used
Increase Small Business Lending (55 percent)	247		\$1,826,180,046
Other Uses:			
Pay Dividends or Redeem Outstanding Equity or Debt	45	\$587,002,316	
Increase Other Lending	65	\$302,251,254	
Held as Non-Leveraged Capital	62	\$258,207,960	
Reduce Borrowings	17	\$146,313,700	
Increase Securities Purchased	21	\$98,574,800	
Other Actions	32	\$73,536,304	
Total Other Uses (45 percent)			\$1,465,886,334
Total Estimated Funding Used			\$3,292,066,380
Unable to Quantify Use	43	N/A	652,194,000
Did Not Complete Survey	9	N/A	83,443,500
Total Funds Disbursed			\$4,027,703,880

* Because respondents could select more than one answer, the sum of responses exceeds the 280 respondents.

Source: OIG analysis of responses

Of the remaining 43 respondents who could not quantify how they used their SBLF funds, 21 were former TARP banks that received a total of \$444 million, and 22 were non-TARP participants that collectively received \$208 million.

Based on Respondent Estimates, 55 Percent of the SBLF Funds Was Used for Small Business Loans

Of the 280 respondents, 246 reported using \$1.8 billion (55 percent) of the SBLF funds awarded them to extend credit to small businesses. More than two-thirds (69 percent) of the 246 respondents stated that having the additional SBLF capital was key to expanding their small business loan portfolios, and 17 percent said they would not have been able to lend money to small businesses without it. Respondents reported that the SBLF capital allowed them to:

- increase lending limits to individual borrowers;
- lend without impairing the institution's Capital-to-Assets ratio;
- enter new markets; and
- gain confidence to lend more.

For example, one bank official commented that "the additional capital cushion provided by the SBLF program provided bank management with a greater degree of confidence to pursue small business lending opportunities in an uncertain economic environment following the recession and financial crisis in 2008."

Even the former TARP respondents that had to repay their TARP investments with all or some of their SBLF funds noted that the change in the nature of the capital, from TARP to SBLF, facilitated increases in their small business lending because respondents

generally considered the SBLF funds to be more stable.⁶ In fact, 66 percent of the former TARP respondents said that SBLF funds were “a more stable source of equity than TARP funding to be used as a base to leverage asset growth with deposits.”

One former TARP respondent specifically commented that “replacing the TARP funds with lower cost, more stable, and less burdensome capital allowed the bank to make a real impact on small businesses in the communities we serve.” Former TARP respondents reported making \$14.3 billion in new small business loans between the date of Treasury’s investment and March 31, 2013.

Based on Respondent Estimates, 45 percent of the SBLF Funds Was Used for Purposes Other than Small Business Lending

Of the 280 respondents that could account for how they spent their SBLF capital, 242 reported using the money in ways that did not extend credit to small businesses, and 34 respondents (24 of which were former TARP banks) did not spend any of their SBLF funds on small business loans. In total, approximately \$1.5 billion (45 percent) of the \$3.3 billion of SBLF capital awarded to the 280 respondents was used for purposes other than making small business loans.

Approximately 40 percent of the \$1.5 billion was used to pay dividends or redeem outstanding debt, according to respondents. Another 38 percent of the \$1.5 billion was spent on loans that were not qualified small business loans or was held as non-leveraged capital.

⁶ Although all of the TARP banks used SBLF funds to pay Treasury back for its TARP investment, 80 of the 131 TARP banks did not report using the SBLF funds to repay debt or equity. Survey responses, comments, and follow-up discussions indicated that the change of the equity from TARP to SBLF facilitated banks’ increases in small business lending.

Half of Respondents Could Isolate the Impact of SBLF and Estimated Using 60 percent of their SBLF Capital on Small Business Loans

As we previously reported, the direct impact that SBLF funds have had on small business lending cannot be isolated from other factors. Because SBLF is a capital investment program and not a direct lending program, the capital invested is leveraged and not traceable to individual loans. Although the direct impact of the SBLF program is not measurable, Treasury evaluates program impact based on the small business lending gains reported quarterly by participants, in accordance with the calculation method prescribed by the Small Business Jobs Act.

We reported that the lending gain measurement established by the Act was solely for the purpose of setting dividend rates, and that it is not an appropriate measure of program impact. In fact, many gains occurred prior to program funding and included loans that were not financed with SBLF funds. Also because the gains reported represent the outstanding quarterly loan balances that participants have on their books, they are heavily influenced by loan payoffs and reductions in loan balances.

Because the reported gains are not all attributable to the SBLF capital that was invested in participants, we asked respondents to estimate the percentage of small business lending gains they reported from the date they received the SBLF funds to March 31, 2013, that was attributable to the SBLF capital. Of the 323 respondents, 151 told us they could not isolate the portion of their lending gains associated with the SBLF capital.

Another 142 respondents said they could, and estimated that \$1.4 billion (or 58 percent) of the \$2.4 billion they reported was a direct result of the SBLF funding. They also stated that at least \$1 billion was not attributable to the SBLF program.

Although Not All Attributable to SBLF, Respondents Reported \$22.8 Billion in New Small Business Lending as of March 2013

Since the SBLF program's objective was to make credit available to small businesses, we asked participants to estimate the amount of new lending they made after they received the SBLF capital. "New lending" differs from what Treasury reports as small business lending gains. New lending constitutes new loans and credit commitments, whereas lending gains that participants report to Treasury in their *Quarterly Supplemental Reports* measure the outstanding loan balances from period end to period end, which are reduced by repayments of loans made prior to the SBLF program.

One of the participant's comments highlighted the difference between new lending activity and "period end" to "period end" lending gains that are used to measure indirect performance for the SBLF program. An official for a median-sized bank (between \$400 million and \$600 million in assets), a former TARP bank, commented: "Although the 'increase' in small business lending was [less than \$1 million] at March 31, 2013 (relative to the baseline), we have originated more than \$37 million in qualified small business loans since SBLF was obtained in August 2011. This was overshadowed, however, by portfolio amortization and higher than expected prepayments in our existing commercial loan portfolio." The \$37 million is new lending.

Almost all of the respondents (98 percent) could estimate the amount of new loans that were made to small businesses after receiving SBLF funding. While not all of the new lending can be attributed to SBLF funding, respondents estimated making \$22.8 billion in new small business loans between the date of Treasury's investment and March 31, 2013.

Of the \$22.8 billion, \$14.3 billion (63 percent) was made by former TARP banks, which collectively received 66 percent of the \$3.9 billion that respondents received in SBLF. Similarly, the non-

TARP respondents reported \$8.5 billion (37 percent) in new small business loans and collectively received 34 percent of the SBLF funds.

This shows that overall both groups were very close in the amount of new lending commitments made relative to the amount of SBLF funds received. The amount of small business lending activity of the former TARP banks was particularly notable as only \$500 million of the \$2.7 billion received constituted new net capital.⁷

While there is no historical data with which to compare new small business lending activity prior to and following SBLF funding, the survey responses would seem to indicate that both former TARP and non-TARP institutions provided significant levels of credit to small businesses while in the program even though former TARP institutions collectively received less SBLF capital than non-TARP institutions. The survey did not explore whether this occurred because both groups had the same loan life cycle or whether it occurred for other reasons.

Because information on new loans and credit commitments may provide an important additional assessment of program impact, Treasury must ensure that such data is accurately reported in its *Annual SBLF Lending Survey* of participants. Currently, this information is unreliable as a significant number of participants reported using different methods of measuring new loans and commitments. For example, when a credit line is increased, only the amount of the increase constitutes new lending, but 109 participants (34 percent) reported the entire line of credit as being new. Additionally, significant changes in loan maturity, shifts between a revolving loan or line of credit, or a change in collateral does not constitute new lending. However, 80 participants (25 percent) reported such changes as new lending. The inaccurate reporting occurred because Treasury did not clearly define new

⁷ The Act required TARP banks to repay their outstanding TARP balances with SBLF capital, which for the participating banks was \$2.2 billion.

loans and commitments before administering its *Annual SBLF Lending Survey*.

Loan Demand, Loan Margins, and SBLF Incentives Influenced Banks to Use SBLF Capital for Small Business Loans

Eighty-two percent of the 323 respondents said that an increase in demand for small business loans was a “somewhat” or “very important” factor in their decision to use SBLF funds to make small business loans. One former TARP bank respondent stated, “We have experienced strong loan demand and SBLF enabled us to meet that demand.” Also important was the ability to achieve sufficient loan margins to obtain an adequate return on such loans. Of those responding, 66 percent reported that being able to achieve sufficient loan margins was important to their decision to make small business loans.

Equally important to the loan margin was the SBLF program incentive, which lowers the SBLF dividend rate as participants increase their small business lending. Sixty-seven percent of respondents reported that the incentive was a “very” or “somewhat” important influence on their use of the funds for small business loans.

For most participants the dividend rate paid quarterly on their outstanding SBLF funding declined from a high of 5 percent to as low as 1 percent as their lending to small businesses increased.⁸ In addition to providing incentive to lend to small businesses, some commented that achieving reduced dividend rates enabled them to offer more competitive rates on loans to small businesses.

The importance of the impact of the program incentive on small business lending is further evidenced by the fact that 80 percent of those surveyed achieved the lowest SBLF dividend as of March

⁸ The 1-percent rate applies to C-Corp banks. S-Corp banks have a 1.5-percent minimum rate and CDLFs have a 2-percent fixed rate.

31, 2013, the end of the OIG survey period. Of those respondents, 38 percent had secured the 1-percent rate with small business lending activity prior to receiving SBLF funds. The ability to maintain the lowest dividend rate continues to incentivize participants to increase their small business lending as 61 percent plan to continue to leverage the SBLF funds to increase returns to their institution.

Other Uses of the SBLF Funds Were Primarily Driven by the Demand for Other Types of Loans and Capitalization Needs

The 156 respondents that reported using their SBLF funds in ways that did not extend credit to small businesses cited various uses of the funds, but primary among them was making other types of loans. Respondents also stated they used the SBLF capital to achieve higher capitalization ratios or meet capital regulatory requirements, while others used the funds for hiring or other activities needed to support increased small business lending.

For those who used the money to make loans to other than small businesses, 84 percent said their decisions were influenced by the demand for such loans. Seventy-nine percent of respondents stated the SBLF funds helped increase their capitalization ratios and 70 percent said they helped them achieve a sufficient loan margin to increase other types of lending. Finally, 63 percent said they used the SBLF capital for other types of lending because of the improving economic conditions or outlook.

More than half (54 percent) of the respondents that reported other uses of their funds said that a downgrade in economic conditions was the primary reason why they did not use their SBLF capital for small business lending. Another 40 percent of respondents said they held their SBLF funds as non-leveraged capital or as reserves, primarily to achieve a higher capitalization ratio.⁹ More than two-thirds of these respondents (68 percent) did so because they

⁹ The capitalization ratio is the percentage of a bank's capital to its assets.

anticipated increases in regulatory requirements for capital reserves. It is important to note that while some respondents did not leverage their SBLF funds, respondents could directly lend the funds without leveraging it. Additionally, achieving higher capitalization ratios positioned the respondents to ultimately make more loans.

Finally, less than a quarter of respondents (22 percent) said they employed the funds primarily to hire new lending personnel or increase their marketing efforts, both of which could facilitate additional small business lending. Specifically, written comments from some institutions stated their marketing efforts included hiring additional loan officers and committing funds to advertising campaigns.

Most Participants Plan to Exit SBLF When the Dividend Rate Resets or Cheaper Capital is Available

Most respondents do not plan to keep their SBLF funds as long-term capital. Of the 319 participants that stated they plan to exit the program, 73 percent said they would leave before the dividend rate resets to 9 percent.¹⁰ Only 6 percent of respondents (16 banks and 3 CDLFs) plan to stay in the program after the rate resets to 9 percent. The 16 banks were evenly split between former TARP and non-TARP banks.

The majority of respondents indicated that the cost of the SBLF capital compared to the cost of replacement capital would determine when they exit the SBLF program. For 96 percent of the respondents, the reset of the dividend rate to an undesirable higher level would expedite their repayment of the SBLF capital. Similarly, 88 percent of respondents reported they would leave the

¹⁰ As described in SBLF program guidance, the dividend rate in the 10th quarter after the closing date is locked in until the end of the 4½-year period after a bank is funded and 8 years after a CDLF is funded. If the capital is not repaid at the end of the period, the rate increases to 9 percent.

program if they could find cheaper capital. Half of all respondents also indicated that they may leave the program if Treasury were to sell the SBLF preferred stock, securities, or equity equivalents that Treasury holds for their institutions.

As of December 31, 2013, 29 financial institutions (28 banks and 1 CDLF) with aggregate investments of \$438 million had repaid SBLF and exited the program, and 2 others had merged with other SBLF participants. Of the 31 institutions that have exited the program or merged with other participants, 19 were former TARP banks. Ten of the banks that exited were large community banks, with assets between \$1 billion and \$10 billion.

Most Respondents Were Satisfied with Program Administration, but 52 Percent of Those Who Rated Their Satisfaction Were Unsatisfied with Treasury’s Handling of Program Fees and Penalties

Most respondents stated they were very or somewhat satisfied with Treasury’s overall administration of the SBLF program. As shown in Table 2, respondents were most satisfied with the dividend rate process, marketing materials, and amount of funds made available under the program. Fifty-two percent of the 98 respondents that rated their satisfaction reported they were unsatisfied with Treasury’s handling of program fees and penalties, and 10 percent or more were unsatisfied with various aspects of the application process, program guidance, and repayment process.

Summarized in Table 2 on the following page are participant comments and satisfaction levels they reported with Treasury’s application process; program guidance and communications; administrative procedures; and assessment of fees and penalties. Because participants did not respond to all of the questions, the number of respondents for each question varied.

Table 2: Satisfaction with Treasury’s Administration of SBLF

	Percent Very or Somewhat Satisfied	Percent Unsatisfied
Application Process		
Amount of Funds Made Available	96%	4%
Timeliness of Application Approval	89%	11%
Ease of the Application Process	89%	11%
Communications and Program Guidance		
Clarity of the Marketing Materials Describing Program	96%	4%
Quality of FAQs or Webinars on Topics of Interest	94%	6%
Clarity of Guidance on the Application Process	92%	8%
Clarity of Program Terms	88%	12%
Level of Responsiveness in Communications	94%	6%
Timely Notification of Certification Filing Deadlines	90%	10%
Resolution of Questions and Concerns	88%	12%
Administrative Procedures		
Handling of the Dividend Rate Process	99%	1%
Management of Quarterly Supplemental Reports	93%	7%
Handling of SBLF Capital Repayment Process	87%	13%
Fees and Penalties		
Handling of Fees and Penalties for Non-Compliance	48%	52%

Source: OIG analysis of survey responses

Application Process – Most respondents stated they were very satisfied or somewhat satisfied with the application process, including the amount of funding, timeliness of application approval, and ease of the application process:

Amount of Funds Made Available: Of those surveyed, 306 (96 percent) reported they were very or somewhat satisfied with the amount of funds made available to them, while 14 (4 percent) were not satisfied. Of the 14 respondents who said they could have used more funds, 8 were CDLFs, 5 were non-TARP banks, and 1 was formerly in TARP. These unsatisfied respondents said they could have used more capital and commented that the work involved to apply to SBLF was not worth the amount received, more funds should have been made available to CDLFs, or the funds were not enough to have an impact.

Timeliness of Application Approval: Almost all respondents (287 or 89 percent) reported they were very or somewhat satisfied with Treasury’s timeliness in approving applications, while 34 respondents (11 percent) said they were unsatisfied. Almost three-quarters of the 34 respondents unsatisfied with the timeliness said the time from application to approval was too long, and they were unable to get information on the status of their applications. Another quarter of the unsatisfied respondents said the application process was overly burdensome, complicated, or lacked transparency.

Ease of the Application Process: Of those who responded, 286 (89 percent) reported they were very or somewhat satisfied with the ease of the application process, while 34 (11 percent) said they were unsatisfied. Most of the unsatisfied respondents stated that the application process was too complicated. Nearly half of these unsatisfied respondents stated they incurred legal expenses to obtain help with their applications and about a third commented that Treasury personnel or designated representatives could not provide answers to their questions.

Communications and Program Guidance – Most respondents said they were very or somewhat satisfied and only a few were dissatisfied with Treasury’s communications and program guidance. As discussed below, respondents rated their satisfaction with Treasury’s marketing materials, *Frequently Asked Questions* (FAQ) and webinars, application guidance, program terms, responsiveness to questions, notification of certification deadlines, and resolution of questions and concerns.

Clarity of the Marketing Materials Describing the Program: Of those who responded, almost all 308 (96 percent) reported they were very or somewhat satisfied with the clarity of the SBLF marketing materials and 12 (4 percent) said they were unsatisfied. The unsatisfied respondents stated the marketing materials were somewhat confusing. Some unsatisfied

respondents described specific problems with the marketing material, such as the baseline calculation for participation loans, S-Corporation requirements, and sex offender documentation.

Quality of FAQs or Webinars on Topics of Interest: In total, 297 (94 percent) respondents reported they were very or somewhat satisfied with Treasury's FAQs and webinars, and 19 (6 percent) said they were unsatisfied. Those who were unsatisfied said the FAQs or webinars didn't cover topics important to respondents, or did not add value. A few of these respondents stated they would have liked more detail, or did not receive notice of the webinars.

Clarity of Guidance on the Application Process: Of those who responded, 295 (92 percent) reported they were very or somewhat satisfied with the clarity of program guidance on the application process, and 26 (8 percent) said they were unsatisfied. The unsatisfied respondents stated that too much interpretation was left to participants, an attorney was needed to explain guidance, the guidance was confusing or cumbersome and that Treasury representatives were not knowledgeable or responsive when asked for clarification. Additionally, some of the satisfied respondents expressed the same concerns.

Clarity of Program Terms: Of those responding, 284 (88 percent) reported they were very or somewhat satisfied with the clarity of the program terms, and 37 (12 percent) stated they were unsatisfied. The unsatisfied respondents stated that the program terms could have better described annual reporting requirements, baseline computations, the time period for dividend rate calculations, TARP bank penalties, acquisitions, annual filings for audited statements, sex offender certifications, S-Corp requirements, administrative reports, and audits of such reports. Some of the satisfied respondents also expressed the same concerns.

Level of Responsiveness in Communications: Ninety-four percent (301) of respondents said they were very or somewhat satisfied with Treasury's responsiveness, and 20 (6 percent) reported that they were unsatisfied. The unsatisfied respondents stated that notifications concerning penalties and non-compliance issues were not timely and that Treasury personnel did not provide comprehensive answers to their questions. Additionally, some unsatisfied respondents stated their communication with Treasury was by email and that direct communication with a person would have been more helpful. Some of the satisfied respondents also commented that Treasury should have been more thorough, provided more reminders and confirmations, advised participants of changes, provided a single point of contact, and answered questions directly, instead of referring participants to guidance.

Timely Notification of Certification Filing Deadlines: Ninety percent (288) of respondents reported they were very or somewhat satisfied with Treasury's communication of the deadlines, while 33 respondents (10 percent) reported they were unsatisfied. Twenty of the unsatisfied respondents stated they received either limited or no notification of filing deadlines for annual reporting requirements, and 10 said they incurred large penalties as a result.

Resolving Questions and Concerns: Of those surveyed, 284 respondents (88 percent) reported they were very or somewhat satisfied and 37 (12 percent) said they were unsatisfied with Treasury's handling of their questions and concerns. Some of the unsatisfied respondents stated that Treasury could have been faster in responding to questions, and that Treasury provided too many points of contact. Other respondents stated that Treasury was not able to completely or reliably answer their questions, especially with respect to annual filings.

Administrative Procedures – Almost all respondents were very or somewhat satisfied with Treasury’s administrative procedures for adjusting dividend rates and managing quarterly supplemental reports, but wanted Treasury to improve the SBLF capital repayment process.

Handling of the Dividend Rate Process: Ninety-nine percent of respondents (307) respondents reported they were very or somewhat satisfied, while 4 (1 percent) stated they were generally unsatisfied. A few of the satisfied respondents found the report deadlines to be inflexible, noting that the process was disorganized in the beginning, and that Treasury had since improved the quarterly report template.

Management of Quarterly Supplemental Reports: Of those who responded, 300 (93 percent) reported they were very or somewhat satisfied with Treasury’s management of the quarterly supplemental reports, while 21 (7 percent) were unsatisfied. Some of the unsatisfied respondents noted delays in Treasury’s responses to questions about the *Quarterly Supplemental Reports*, and thought the Department’s review of these reports was overly detailed and cumbersome. A few of the satisfied respondents said that Treasury had improved the reporting process over time.

Handling of the SBLF Capital Repayment Process: Forty respondents (87 percent) reported they were very or somewhat satisfied, while 6 (13 percent) stated they were unsatisfied with the process for repaying the SBLF capital. At the time of the survey, only 15 participants had exited the program. Five of these respondents reported the exit process took too long and was too complicated.

Fees and Penalties – Of the 98 participants that rated their satisfaction with the administration of fees and penalties, 47 (48 percent) reported they were very or somewhat satisfied with Treasury’s handling of fees and penalties, while 51 (52 percent)

were unsatisfied. Of note, 49 respondents¹¹ stated that the fees and penalties were excessive, caused them to file appeals, or could have been avoided had Treasury sent notice of the annual certification deadline. The respondents that complained paid an average of \$78,600 each in fees and penalties.¹² Of those respondents, a few stated that Treasury's penalty structure was inequitable.

Recommendation

We recommend that the Deputy Assistant Secretary for Small Business, Housing, and Community Development establish a clear definition of new loans and commitments made to small businesses before administering the next *Annual SBLF Lending Survey* so that the Department has reliable data with which to assess the impact of the SBLF program.

Management Comments and OIG Response

We provided a draft of this report to Treasury on March 12, 2014, and received formal written comments on March 26, 2014. Treasury accepted the recommendation and noted that it provided additional guidance to participants regarding the definition of new lending in the program's second *Annual SBLF Lending Survey*.

Treasury expressed concern with two findings. SBLF's Director said the report's statement that "52 percent of those who rated their satisfaction were unsatisfied with Treasury's handling of program fees and penalties" may mislead some readers. He stated that if the approximately 200 respondents who indicated that fees and penalties did not apply to them were included in the calculation

¹¹ Two respondents reported they were unsatisfied with Treasury's handling of fees and penalties, but did not elaborate.

¹² Twelve banks made comments about specific dollar penalties in response to the survey. The penalties ranged from about \$4,000 to more than \$300,000. The median penalty was \$37,961.

of the satisfaction rate, only 51 of 321 respondents, or 16 percent, would be dissatisfied with fees and penalties. Additionally, he stated that Treasury does not charge “fees and penalties,” but denies dividend rate reductions to financial institutions that do not submit valid annual certifications of small business lending, and “it seems logical that institutions that did not receive this economic benefit because of their non-compliance may be dissatisfied with that outcome.”

Second, the SBLF Director expressed concern that the report’s finding that “only an estimated 55 percent of the awarded funds went to small business loans,” is unreliable because respondents may have used different methodologies in making their estimates. He also stated that the SBLF funds cannot be directly linked to specific uses. A formal written response from Treasury is included in its entirety in Appendix 2.

We consider Treasury’s action to be responsive to the audit recommendation. Regarding Treasury’s concern about the reported percentage of respondents that were dissatisfied with its handling of fees and penalties, we believe that calculating the dissatisfaction level in the manner Treasury suggests would indeed mislead readers. Adding the 221 who responded “not applicable” to the percentage dissatisfied would inappropriately infer they were satisfied with the penalty process. We believe it would be akin to asking participants who are still in the program to rate their satisfaction with the process for exiting the program. Therefore, we believe reporting that 52 percent of the 98 respondents who experienced fees and penalties were dissatisfied with them is the only appropriate way to convey those results.

Regarding Treasury’s concern about the accuracy of respondent estimates of the percentage of awarded funds that went to small businesses, we agree that respondents may have employed divergent methodologies in producing their estimates, and we previously made the appropriate disclosures in the report.

We appreciate the courtesies and cooperation provided to our staff during the evaluation. If you wish to discuss the report, you may contact me at (202) 622-1090, or Clayton Boyce, Audit Director, at (202) 927-5642.

/s/

Debra Ritt

Special Deputy Inspector General for

Office of Small Business Lending Fund Program Oversight

Appendix 1: Objectives, Scope, and Methodology

The objectives of the audit were to: (1) determine how recipient institutions are using funds awarded under the Small Business Lending Fund (SBLF) program and the factors that most influenced their use of funds; (2) determine participants' plans to repay Treasury's investment and exit the program; and (3) evaluate Treasury's administration of the program.

To accomplish our objectives, we conducted a survey of 325 of the original 332 SBLF participants. We excused seven participants from the survey because five had merged with other banks and two had requested not to participate. Of the 325 participants surveyed, 323 responded, including 9 that had exited the program, for a response rate of 99 percent. Our survey had 145 separate questions or requests for data among 20 questions. We took steps to minimize non-sampling errors by pre-testing the questionnaire with 5 banks in April 2013, with a representative of each business entity type. We conducted the pretests to make sure that the questions were clear and unbiased and that the questionnaire did not place an undue burden on respondents. We implemented a number of changes based on the pre-test comments and finalized the survey in April 2013. Most data supplied by participants was as of March 31, 2013, or earlier. Some questions about the participants' experience with Treasury in applying to the program related to early 2011.

To help increase the response rate, the Office of Inspector General (OIG) obtained the most recent updated list of SBLF participant contact names and addresses from Treasury, and also sent a notification e-mail to each participant informing the participants that we would be sending out the survey the following week and requesting the contact information for the best person to receive the survey. In May 2013, we received clearance from the Office of Management and Budget to administer the survey. The team distributed the survey to all SBLF participants by e-mail using an electronic fillable Adobe file on June 11, 2013.

The OIG used Adobe software to administer the electronic surveys to help minimize data input issues. We validated the survey results using check-in procedures that were designed to find errors or inconsistencies. We followed up with the participants as necessary for missing, incomplete, or inconsistent data. Many of the survey questions were multiple choice. Eight survey questions asked respondents to fill in comment boxes. We created a series of demographic fields, including participant's qualified loan growth performance, entity type, Troubled Asset Relief Program (TARP) participation, asset size, and SBLF dollars funded. We created a database and ran frequencies and queries on the data using statistical software. The team consulted with OIG's statistical expert throughout the survey process.

To accomplish our first objective, we asked participants how they used their SBLF funds from the quarter in which participants received Treasury's investment (the quarter ended September 30, 2011, for all but 4 participants) to March 31, 2013. We asked participants how they distributed their SBLF funds among 11 categories of uses, how SBLF funds allowed their institution to increase the availability of credit to small businesses or why they did not increase small business lending. We also asked them to estimate how much the funds increased their small business lending and to identify the factors influenced the participants to use their SBLF funds in a specified way. We reported the estimates provided, although respondents may have used different methodologies in estimating how they used their SBLF funds.

To accomplish our second objective, we asked participants for their plans to repay Treasury's investment and exit the program. To accomplish our third objective, we asked participants if they were satisfied with Treasury's rollout, initial execution, and administration of the program. We then compared the responses for all three objectives among subgroupings of respondents defined by TARP participation, asset size, and type of business entity, and analyzed the results.

We conducted our audit from March 2013 to January 2014 in Washington, D.C., in accordance with *Government Auditing Standards*. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained to address our audit objective provides a reasonable basis for our findings and conclusions.

Appendix 2: Management Response



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 26, 2014

Debra Ritt
Special Deputy Inspector General for
Office of Small Business Lending Fund Program Oversight
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Dear Ms. Ritt:

Thank you for the opportunity to review your draft report (the Report) titled "Survey of Small Business Lending Fund Participants on Use of Program Funds, Repayment Plans, and Satisfaction with Treasury's Program Administration." This letter provides the Department of the Treasury's (Treasury) official response.

The Report examines the responses of nearly all SBLF participants to a survey conducted by the Office of the Inspector General. We are pleased that the Report found that 89 percent of the survey respondents were satisfied with Treasury's administration of the SBLF program. In addition, most survey respondents indicated that, as planned, they anticipate repaying Treasury's investment and exiting the program before the dividend rate resets rather than retaining SBLF funding for a longer period. Taken together, the Report's findings provide further evidence that the SBLF program is working as intended and that Treasury has administered the program in an effective manner.

We have previously shared our concerns regarding two of the Report's findings. First, we believe that the Report's statement that "52 percent of those [respondents] who rated their satisfaction were unsatisfied with Treasury's handling of program fees and penalties" may be misleading to some readers. The survey question in which OIG asked respondents to rate their satisfaction in this regard directed respondents to "check [a separate box] if this area is not applicable to your institution" (*see* survey question 19(h)). Any such "fees and penalties" applied only to institutions that did not comply with certain contractual terms of Treasury's investment.¹ Accordingly, it appears that only 98 of the 323 survey respondents reported a level of satisfaction with this element of the program, with 47 reporting that they were satisfied, 51 reporting that they were unsatisfied, and approximately 200 indicating that "fees and penalties"

¹ Treasury notes that the survey's use of the phrase "fees and penalties" is inconsistent with the SBLF program terms. Treasury does not charge "fees and penalties" to program participants. However, participants are contractually required to submit valid annual certifications to Treasury to receive the benefit of the dividend rate reduction offered to institutions that increase small business lending. Separately, it seems logical that institutions that did not receive this economic benefit because of their non-compliance may be dissatisfied with that outcome.

did not apply to them. If assessed on the basis of all respondents – rather than merely the subset of respondents for which “fees and penalties” applied – just 16 percent (51 of 323 respondents) reported dissatisfaction with the administration of this provision of the program.

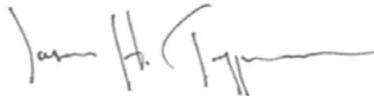
Second, we are concerned that the Report’s finding that “only an estimated 55 percent of the awarded [SBLF] funds went to small business loans” and its related commentary relies on inherently unreliable data. OIG’s survey asked respondents to “estimate” their allocation of SBLF capital to various uses, but it did not provide respondents with a methodology for deriving such an estimate, nor did it request that respondents describe the methodology they used. We are unaware of an industry or accounting standard that respondents could have used to derive such estimates. Indeed, such a standard is unlikely to exist because the fundamental principles of double entry bookkeeping do not permit a direct linkage between individual dollars of equity and specific corporate activities.

Because of the lack of a standard methodology for estimating a participant’s use of SBLF funds, there is a high likelihood that participants used inconsistent approaches to derive their estimates. This is evidenced by the fact that the results for these questions appear to contain significant irregularities. For example, while all former TARP participants were required to use their SBLF funding to redeem TARP investments, the Report states that 61 percent of respondents that were former TARP participants did not indicate that they had used SBLF funds to repay any debt or equity (which would include repayment of TARP financing), while 39 percent reported that they had used SBLF funds in this manner. In this instance, banks that were similarly situated seem to have provided widely divergent responses. In view of such clear inconsistencies in the underlying responses, Treasury is concerned that the Report’s aggregation of these disparate inputs into combined dollar and percentage estimates of SBLF capital usage may produce unreliable conclusions.

With respect to the Report’s sole recommendation, Treasury notes that it provided substantial additional guidance to participants regarding the definition of new loans and commitments in the program’s second annual lending survey, the results of which will be published later this year. We accept the Report’s recommendation to further clarify these definitions in subsequent surveys.

Thank you once again for the opportunity to review the Report. We look forward to working with you and your team in the future.

Sincerely,



Jason H. Tepperman
Director
Small Business Lending Fund

Attachment

Appendix 3: Major Contributors

Debra Ritt, Special Deputy Inspector General

Clayton Boyce, Audit Director

Anita Visser, Audit Manager

Karin Beam, Auditor-in-Charge

Bill Malloy, Auditor

Kimberly McKeithen, Referencer

Appendix 4: Distribution List

Department of the Treasury

Deputy Secretary
Office of Strategic Planning and Performance Management
Risk and Control Group

Office of Management and Budget

OIG Budget Examiner

United States Senate

Chairman and Ranking Member
Committee on Small Business and Entrepreneurship

Chairman and Ranking Member
Committee on Finance

Chairman and Ranking Member
Committee on Banking, Housing and Urban Affairs

Chairman and Ranking Member
Committee on Homeland Security and Governmental Affairs

Chairman and Ranking Member
Appropriations Subcommittee on Financial Services and General
Government

United States House of Representatives

Chairman and Ranking Member
Committee on Small Business

Chairman and Ranking Member
Committee on Financial Services

Chairman and Ranking Member
Committee on Oversight and Government Reform

Chairman and Ranking Member
Appropriations Subcommittee on Financial Services and General
Government

Government Accountability Office

Comptroller General of the United States