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Examination of 7(a) Loans to Poultry Farmers

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Thank you, Chairman Chabot and Ranking Member Velazquez. I appreciate the opportunity to talk to you about poultry loans and the Agency's 7(a) lending history.

The March 2018 Inspector General report examined loans made to poultry growers during Fiscal Year 2012 to Fiscal Year 2016. From their examination, the IG issued two recommendations to the Agency, both of which SBA agreed with.

First, SBA was asked to look at eleven loans that served as the sample size and basis of the Inspector General's review. Second, SBA was asked to consider further guidance to ensure that appropriate determinations of affiliation are being made.

The loan activity highlighted by the Inspector General occurred over a five year span, beginning seven years ago. I came on board at the Agency to lead the Office of Capital Access in March of 2017. Accordingly, for questions about the Agency's poultry loan history, particularly during that five year timeframe, I will need to rely on program office background and data.

Before getting to the two IG recommendations, let me give you a general overview of lending in our 7(a) program, both past and present.

Today, our overall 7(a) loan portfolio – all categories – has a loan count of just over 265,000 loans (265,014) and an outstanding balance of $88.1 billion.

Within that, poultry loans represent just 1% of the entire 7(a) portfolio. During the FY2012 to FY2016 period, the number of poultry loans approved by lenders and SBA totaled 2,201, with a corresponding value of $1.88 billion.

The average approved amount of poultry loans ranged from $521,000 in FY2012 to just over $1 million in FY2016.

The performance of poultry loans has been very good. Those loans have a delinquency rate of less than one-half of one-percent (0.34%). This compares to the 7(a) average of 0.64%.

Examples of the type of loans made during this time are of a $600,000 loan to a Kentucky couple who were employed in farming but wanted to start their own business, and a $1 million loan in Mississippi to save a local family owned, but failing, poultry operation.

With that as a foundation, let's turn to the two IG recommendations and SBA's response. As mentioned, we were asked to look at the eleven loans cited in the evaluation sample and, more generally, at the arrangements between integrators and growers. As Associate Administrator for Capital Access, I was asked to determine if our staff, and lenders, made a proper size determination on the eleven loans. If not, it was recommended that we take corrective action.

Soon after the release of the IG report, my office reviewed the eleven loans and found that the loans were properly made, in accordance with SBA policy and procedure at the time. We are also reviewing the arrangements between integrators and growers and will determine whether supplemental guidance is needed to ensure that appropriate affiliation determinations continue to be made.

The IG report questioned whether the nature of the agreement between the poultry grower and the business supplying the chicks is so controlling that SBA should consider the two businesses to be affiliated. This concept of affiliation is relevant in determining whether a business is small because the size of a business is determined by aggregating the revenues or employees of the business with those of all of its affiliates. As you know, only businesses that are small are eligible for financial assistance under SBA's general business loan programs.

In accordance with the Small Business Act, SBA makes financial assistance available to certain poultry farmers and other agricultural enterprises. Although it is the mission of the Department of Agriculture to assist farm businesses in rural America, Congress also specifically included agricultural enterprises in the definition of small business for purposes of SBA's general business loan programs. Agricultural enterprises are identified under the NAICS code system as including poultry and egg; forestry and logging; cattle ranching; and hog and pig farming, to name a few.

As the IG report noted, SBA has taken the position for many years that the poultry grower-integrator contract, standing alone, does not bring about affiliation. Recently, in the last Administration, the SBA rules governing affiliation in the business loan programs were narrowed. The Agency removed from the affiliation regulations the provision that considers contractual relationships that may cause economic dependence of one business on another.

The Agency concluded that, in general, only firms that had common ownership, or common management, should be considered affiliated when determining eligibility for SBA financial assistance. As a result, SBA's current regulations do not consider whether the contract between an integrator and a poultry farmer results in economic dependence when determining the size of the poultry farmer that applies for financial assistance.

The Office of Capital Access is currently evaluating our policies to determine if any modifications are needed. Soon after joining the SBA, I began an examination of various loan policies and practices in my office. As an example, on the topic of franchise lending, we ultimately implemented changes that were incorporated into the program last year, all of which have been well received by borrowers, lenders and other interested parties. As we continue to conduct our review of poultry lending, we want to hear from all stakeholders, and I would certainly welcome the views of this Committee and your Senate counterparts. If, for this specific area of lending, modified policy guidance is appropriate, then we would want to shape that with your input.

Thank you for the opportunity to testify today. I look forward to working with you.