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Small Business

Money Store Presses Senators To Influence SBA Final Rule, Source Says

The largest maker of loans backed by the Small Business Administration is pressuring members of Congress to influence agency officials not to publish regulations that could require the corporation to increase its reserves when it sells the unguaranteed portions of small-business loans, according to a Senate source.

The source told BNA that the Money Store Inc. has consistently asked members of the Senate to press SBA not to promulgate regulations requiring lenders to keep a 5 percent stake during the securitization of the unguaranteed portions of these loans. The loans involved are known as 7(a) loans.

"There is clear evidence from the lobbying efforts of the Money Store that the company is obviously around the Senate to drum up support for their position," the Senate source contended.

An SBA official denied the accusation, telling BNA that allegations the Money Store has pushed for the agency to delay publishing any regulations are "totally without foundation."

According to industry observers, the financial institution may be wary of increasing reserves because the securitization process enables non-bank lenders such as the Money Store to finance additional loans, a key factor in replenishing capital. Mandating reserves could reduce the corporation's profits.

"Any time a financial institution is required to hold back capital, those are funds that can't be used to generate income," an SBA official stated.

A Money Store official said Jan. 6 that the corporation "is not trying to block a regulation." The official said the Money Store wants to ensure that a final rule does not pose undue risks to taxpayers.

Bond Calls For Suspension

Senate Small Business Committee Chairman Christopher Bond (R-Mo) recently asked SBA to suspend the feature of the 7(a) guaranteed loan program allowing lenders to bundle and sell the unguaranteed portions of these loans.

Bond sent a letter to SBA Administrator Aida Alvarez requesting the agency not pledge, securitize, or grant any further approvals of sale of the unguaranteed portions of 7(a) loans until Congress has an opportunity to examine the issue.

Alvarez responded in a letter to Bond that she is "committed" to ensuring the safety, soundness, and effectiveness of the SBA 7(a) program and the agency is refining the securitization process. A final rule is expected by spring, she noted. However, Alvarez said the agency is very reluctant to suspend the feature of the 7(a) guaranteed loan program allowing lenders to bundle and sell the unguaranteed portions of these loans.

During the committee's examination, Bond said he and his colleagues will consider the necessity of the feature of the loan program allowing lenders to securitize the unguaranteed portion of the loan. Bond's two-page letter, obtained by BNA, suggested the questionable actions by the agency could adversely impact the "safe and sound" operation of the small business finance program.

The safety and soundness of the SBA 7(a) guaranteed loan program has recently become a point of contention, with some industry observers and congressional sources criticizing the SBA's alleged preferential treatment of its largest lender, the Money Store. These sources believe political pressure has caused the SBA to delay a final rulemaking that could impact the reserves of lenders.

Question of Money and Influence

Campaign finance reports show that the Money Store and individuals connected with the financial institution have made numerous political contributions since 1995. Figures reported to the Federal Election Committee were analyzed at BNA's request by the Center for Responsive Politics, a nonprofit, nonpartisan research organization that studies campaign finance issues. The FEC reports show that the Money Store and individuals connected with the company made nearly $425,000 in political contributions during the 1996 election cycle and contributed another $40,000 in 1997.

Of the 1997 contributions, nearly all were soft money donations to Democratic Party committees. The Money Store gave $25,000 in soft money to the Democratic Senatorial Campaign Committee last May 12 and gave another $15,000 to the Democratic Congressional Campaign Committee on June 6.

Of the 1995-96 contributions, over $73,000 was in hard money contributions, mainly to congressional candidates. Democratic candidates received $27,500, while Republican candidates received $41,250.

The Money Store also gave $350,000 in soft money in the last election cycle. The Democratic Party got $255,000, while the GOP got $95,000.

Hard money refers to contributions within the limitations and prohibitions of federal campaign finance laws, which can be used to directly support candidates. Soft money includes largely unregulated contributions to the political parties, supposed to be used for "party-building" activities.

SBA Decries Accusations

Eugene Carlson, associate administrator and spokesperson for the SBA, told BNA Dec. 16 that accusations the Money Store has pressed the agency to delay a final rule are without foundation.

"The delay precipitating the final rule was made by the administrator to ensure SBA had adequate risk assessment criteria in place within the securitization program," Carlson stated.

Carlson said a final rule, which a source said mandated a 5 percent reserve was presented March 31 to the new administrator, Alvarez. After reviewing the rulemaking, Alvarez issued an interim final rule. Unlike the final rule presented to Alvarez, a source said the interim final rule permits the sale of unguaranteed loans in some cases without, the 5 percent reserve. The Senate source called the measure issued in April a "watered down" ruling.

Under the interim final rule, Carlson said someone who conducts a securitization and holds back 5 percent would be given favorable review by the agency. Transactions not meeting the 5 percent retainage "benchmark" would be approved by the SBA on a case-by-case basis.

Securitization Process

In explaining the relationship between the SBA and a lender, Carlson said the lender makes loans to small businesses much like a bank. The small business must first go to a bank, and if turned down, the business can apply for an SBA-guaranteed loan under the 7(a) program. The small business can then ask the lender to guarantee up to 80 percent of loans up to $100,000 and 75 percent of loans up to $750,000.

During the securitization process, he said the lender takes the unguaranteed portions of the loans, packages them together into a security, and sells them on the secondary market. The money from the sale is then used to finance additional loans.

Five securitizations have been approved since the issuance of the interim final rule. According to the SBA spokesperson, the agency approved a $51.3 million loan sale by Sierrawest Bank in June, a $34.3 million loan sale by Independence Funding Corp. in November, and a $140 million loan sale in September by the Money Store. More recently the agency has approved a $21.5 million loan sale by Emergent Capital and a $19.8 million loan sale by Business Loans Center.

Unlike the others, the Money Store's sale was approved with zero retainage upon investigation by the SBA. Sources agreed the Sierrawest Bank securitization was approved with a 5 percent retainage and the Independence Funding Corp. securitization was approved with a 2.5 percent retainage. Both the Emergent Capital and the Business Loans Center securitizations were also approved with approximately a 2.5 percent retainage.

Carlson said the agency approved the Money Store's loan sale on the basis of the safety and soundness of the corporation's record.

"The Money Store has done a number of securitizations over the years with SBA, and they all have had zero retainage," Carlson stated, adding both approvals are consistent with the interim final rule.

Responding to actions taken by the SBA, Bond has stressed the agency should treat all its lenders equally with " clear, open, and predictable rules" for securitizing the unguaranteed portions of 7(a) loans. Such requirements are established by a provision included in Public Law 104-208, he added, and are needed to protect the safety and soundness of the 7(a) guaranteed loan program as well as to protect taxpayers from exposure to excessive risk.

Morton Dear, chief financial officer of the Money Store Inc., told the SBA during a formal hearing last May the current securitization structures, which include the investment grade ratings approach, are more efficient than the proposed regulation calling for a 5 percent reserve.

While the 5 percent reserve would better protect the SBA on an individual securitization, Dear said the lender would be weakened by not having the reserved funds available for other operations. In addition, Dear said a 5 percent hold-back would shrink securitizations by at least 20 percent. This would force lenders, particularly non-bank lenders, to finance the remaining unguaranteed portions through costly bank lines of credit, he stated in written testimony.

"These increased costs ultimately flow back to the small business owners," Dear stressed.

The agency plans to revisit the interim final rule in 1998, Carlson said. He declined to specify whether or not 5 percent retainage would remain in any future rulemaking.

By Arnesa Howell