Testimony of

Edward C. Ashby, III

On behalf of the

American Bankers Association

before the

Subcommittee on Investigations, Oversight, and Regulations

of the

Committee on Small Business

United States House of Representatives

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Chairman Kelly, Ranking Member Adams, and members of the Subcommittee, I am Ted Ashby, President and CEO of Surrey Bank & Trust. Surrey Bank is a community bank headquartered in Mt. Airy, North Carolina with $278 million in total assets. I appreciate the opportunity to present the views of the American Bankers Association (ABA) on the state of the Small Business Administration's (SBA) 7(a) Loan Program and the importance of this program to my community and banks like mine. The ABA is the voice of the nation's $16 trillion banking industry, which is composed of small, mid-size, regional and large banks that together employ more than 2 million people, safeguard $12 trillion in deposits and extend more than $9 trillion in loans.

Our bank was chartered in 1996 with a focus on business lending. At my bank, as is true of my banker colleagues around the country, we are intensely focused on building and maintaining long-term relationships with our customers. We view our customers not as numbers but as individuals and business owners. The success of Surrey Bank is inextricably linked to the success of the communities we serve. They are, after all, our friends and neighbors.

Small businesses are an engine of growth and job creation for the U.S. economy. In order for small businesses to grow, they require safe and reliable funding. Community banks in particularly focus intensely on small business lending. According to the FDIC, community banks increased small loans to businesses (defined as less than $1 million) at more than twice the rate of non-community banks in 2016 and account for 43 percent of all small loans to businesses.

The SBA programs are an important part of business lending for many banks. It helps fill a critical gap, particularly for early stage businesses that need access to longer-term loans. The guarantee helps reduce the risk and capital required for banks and facilitates loans that might never have been made without this important level of support.

In 1999, Surrey Bank began using SBA and other government sponsored credit enhancement programs as a tool in its strategy of helping local companies meet their credit needs. As a portfolio lender, this allowed our bank to attract a wider range of customers and improve the financial condition of the bank. SBA granted Surrey Bank its Preferred Lender Status in 2003 after determining the bank had sufficient experience and resources to properly administer the program. Since that time, the bank has actively participated in the SBA 7(a) Loan Program and has earned "Community Bank of the Year" award in North Carolina twelve of the past fourteen years.

Participation in the SBA 7(a) Loan Program is an integral part of our business model as a commercial bank. The bank has $212 million in outstanding loans, of which about 67% (or $142 million) is for business related purposes. Currently, the bank has $34.7 million in SBA loans of which $26.5 million is guaranteed by SBA. Thus, a total of 18.7% of our business related loans and 12.5% of all loans have SBA guaranties.

The success of the SBA 7(a) Loan Program for my community and Surrey Bank is evident by the 174 active loans with an average loan size is $199,366. As an example, the bank extended credit to a pre-cast concrete company that opened in 2007. Economic activity was far below expectations and the borrower experienced difficulty generating working capital to invest in new work orders. The bank used SBA's Cap Lines Contract Loan Program to fund the individual orders. This company now generates sufficient cash flow to funds its operations without SBA or bank assistance. Also, the bank extended credit to a start-up operation engaged in traffic and safety control for highway and bridge construction. The company started in 2004 with four employees and two trucks. Since inception, the bank has extended them 23 SBA loans over 12 years to fund expansion. The company now has annual revenue over $12,000,000, a fleet of over one-hundred vehicles and 90 employees. Our success is replicated over and over across communities in this country. This is why ABA supports the Small Business Committee's effort to build on the positive aspects of the Program and consider improvements that would benefit the business community.

In my comments below, I will outline some of the positive aspects of the program and provide some suggestions for improvements to make the program even more effective.

Positive Aspects of SBA 7(a) Loan Program

Let me begin by complimenting the staff in the SBA's North Carolina District Office. Our bank has received a high level of support and encouragement from District Director Lynn Douthette and her staff. The professionalism and dedication to help small businesses and banks is part of the equation of success of the SBA programs. In addition, the complementary local programs, particularly the free counseling through SCORE (Service Organization of Retired Executives) has proven very helpful in mentoring business clients.

Here are some key features of the SBA Program that are very positive:

- The Express Loan Program is very effective. It reduces the level of paperwork, utilizes the internal loan policies of the originating bank and reduces the cost of the transaction to the small business customer.
- Loans to start-up businesses require a business plan as part of the approval process. This requirement has proven very useful in helping the owner to consider various facets of the business that are essential to achieve profitability and grow the company.
- The program allows the use of projections in start-up businesses to underwrite cash flow to support the credit request. Under conventional financing, banks would normally require an abundance of collateral or a guarantor with a high level of liquidity to grant credit.
- The credit score generated by the SBA software to determine eligibility is very helpful in providing fast response times to prospective borrowers.
- The program provides for extended loan amortizations on secured loans at a higher percentage of the useful life of the collateral. This improves the borrower's cash flow.
- The advance rates on secured loans are higher than general loan policy. This reduces the amount of working capital a small business needs to invest into the fixed assets of the business.

- The program provides for a long-term loan commitment without the time, expense and uncertainty associated with of balloon payments typically used in conventional financing.

- Loans can be underwritten based on cash flow without relying on collateral coverage or book equity in the business as a condition for credit.

- The use of "Delegated Authority" for Preferred Lenders allows the bank to modify loans. This provides the borrower an opportunity to work through short term cash flow issues and or reschedule debt payments without being forced into liquidation.

- Veterans enjoy reduced fees on loans between $150,000 and $700,000.

Opportunities for Improving the SBA 7(a) Loan Program

Below are some examples of how the program can be improved, primarily relating to the servicing of SBA loans:

- SBA loans cannot be consolidated or refinanced by the same lender. In instances where the borrower is experiencing rapid growth, the bank is required to make multiple loans on the same collateral. Frequently, loans are cross collateralized, which make extending additional loans more complex. Servicing and administration of the loans is difficult for the borrower and the bank.

- SBA guidelines no longer allow a bank to obtain a guaranty to avoid regulatory loans-to-one-borrower limitations. This is a disadvantage to small banks that are portfolio lenders attempting to meet the credit needs of customers in their market. A carve-out for banks that are under $1 billion in assets engaged in portfolio lending should be considered.

- The use of subcontractors in the liquidation process at times resulted in confusion over the correct version of the Standard Operating Procedures (SOP) used to determine eligibility for repurchase. This caused delays in the liquidation process. We suggest sub-contractors receive additional training on identifying the appropriate SOP in affect when the loan was originated.

- A loan is liquidated based on the type of loan program. When a borrower has multiple loans, liquidation can involve multiple service centers in different states. This creates a duplication of work for the bank. More importantly, borrowers have a difficult time making an "Offer in Compromise" until all claims are processed.

- The SBA One platform is not fully operational, which results in duplication of work to produce the forms required to properly close the loan.

Conclusion

The health of the banking industry and the economic strength of the nation's communities are closely interwoven. We strongly believe that our communities cannot reach their full potential without the local presence of a bank—a bank that understands the financial and credit needs of its citizens, businesses, and government. The SBA 7(a) Loan Program is a success and should be vigorously supported in the future. It has encouraged economic growth in our community and allowed Surrey Bank to meet the credit needs of many small businesses. The positives of the program are many and the areas of improvement are primarily related to servicing aspects of the program.

Before closing, I want to express the concern shared by many of my banking colleagues that the community banking model we know today will collapse under the massive weight of rules and regulations. Lack of earning potential, regulatory fatigue, lack of access to capital, limited resources to compete, inability to enhance shareholder value and return on investment, all push community banks to sell. The Dodd-Frank Act has driven all of these in the wrong direction and is leading to consolidations with very real consequences for local communities.

Last year 251 banks disappeared; since Dodd-Frank was enacted, nearly 2,000 banks have merged or closed their doors. For community banks, it goes beyond just our parochial interests. We are very much a part of our community. It is why every bank in this country volunteers time and resources to make their communities better. If the relentless pressures on our small banks are not relieved, the loss will be felt far beyond the impact on any bank and its employees. It will mean something significant has been lost in the community once served by that bank. This is why it is imperative that the Administration and Congress take steps to ensure and enhance the banking industry's capacity to serve their customers, thereby facilitating job creation and economic growth.