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Small businesses run up big debt

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Do you like the food at Quiznos and Cold Stone Creamery? Your taxes have been subsidizing franchises of those companies whether you eat there or not.

A recent study found that operators of those restaurants received millions of dollars in loans through the federal Small Business Administration program, but were among those most likely to leave taxpayers holding the bag by defaulting. Overall, bad SBA loans have cost taxpayers $1.3 billion since 2000, demonstrating the dangers of government picking winners and losers.

The SBA has been around for 60 years, and was launched with a noble intent: helping people to start a business. But as with many government programs, it can have the effect of encouraging riskier behavior by guaranteeing that the feds will step in if needed. Just as banks were encouraged by government mandates and guarantees to loosen standards for mortgages in the early 2000s, leading to the 2008 economic meltdown, observers say lenders were sometimes too quick to grant SBA-backed business loans.

"There were an awful lot of people who got small-business loans during this period 2004 to 2007 that shouldn't have gotten them," Pat Newcomb, director of the Ohio Small Business Development Center at the Entrepreneur Center in Dayton, told the *Dayton Daily News*, which did the study. "They were a bad loan when they were made. They just got worse."

More than 1 million loans have been guaranteed since 1990 under the SBA's 7 (a) program, its most commonly used type of loan. After removing loans that are still active, more than 20 percent of the remaining loans were discharged to the U.S. Treasury after the borrowers defaulted and collection efforts by the lender and the SBA failed. Once a loan reaches that status, there is almost no chance that the government will collect; the *Daily News* says the Treasury's average annual recovery rate on referred loans between 2010 and 2012 was 0.63 percent.

Of more than 160,000 loans that were charged off as unrecoverable, more than half failed before 20 percent of the loan was repaid. In more than 1 in 3 cases, just 10 percent or less of the loan was repaid. And more than 7 percent of the time, the borrower did not pay down the principle at all before defaulting.

One issue, of course, is that SBA-backed loans by definition are considered somewhat risky. That's why they're going through the SBA in the first place. In 2011, the conservative Cato Institute found that between 2001 and 2010, restaurants were by far the leading type of business granted an SBA loan. Since restaurants are widely known to have a high failure rate, it shouldn't come as a surprise that this sector also had the highest rate of default on SBA loans.

Most borrowers do repay their SBA loans, and proponents argue that there remain good reasons to support the program.

Data such as this, though, are a reminder that constant oversight is needed to ensure that a hand up doesn't become a handout at taxpayers' expense.