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THE PLAYBOOK

SBA approved millions of loans during Covid. It now sits at the center of a bankruptcy wave.



Small businesses across the country took on debt to stay afloat during the Covid-19 pandemic. It might be hard to get out from under it.

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Robert Andelman keenly remembers when the Covid-19 pandemic cut his business off at the knees.

Andelman, the owner of screen-printing, dye and sewing firm Nightmare Graphics in Columbia, Maryland, lost nearly all of his orders on March 13, 2020, as the pandemic began to spread across America. He did what many business owners did and pivoted to making masks. The market kept changing, so he did as well.

He also took advantage of the Small Business Administration's Paycheck Protection Program, introduced in 2020 during the pandemic, to keep his workers on the payroll, hoping the industry would recover.

Then came the Omicron variant of Covid-19 that swept the country in late 2021 and early 2022, which knocked his business down for the count. Revenue, which had topped more than \$5 million annually, dropped by more than half, to just \$2 million. Before the pandemic, Nightmare Graphics had 32 employees. Today, has just 16.

Andelman signed up for an SBA Covid Economic Injury Disaster Loan, which carried a 30-year term at a low interest rate. The program was designed to help small-business owners access capital while many banks pulled back.

But instead of getting the \$1 million he was approved for – and needed – Andelman got \$500,000 just as the loan program unexpectedly shut down for good, when the SBA said it no longer needed to be funded. Andelman turned to high-interest loans to stay afloat. He also gave up his lease and moved to a cheaper space.

“We were looking pretty good up until that point, and then it was just a mess,” Andelman told The Playbook. “The loan we got just covered our move and our back rent to our previous landlord.”

Eventually, Andelman pulled the trigger and filed for bankruptcy, only to find there wasn't going to be much relief from his EIDL loan or his smaller, traditional SBA 7(a) loan he had taken out before the pandemic to purchase the business.

The SBA guarantee it offers in its 7(a) program only covers lenders after they have made every attempt to recover as much as they could from

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a business' assets. Meanwhile, Andelman was unable to discharge the EIDL loan as part of his reorganization effort. That means while Andelman was able to discharge some of his debts, his SBA loans still loom large. And, he said, the SBA was largely uncommunicative during the process. They offered him a pause on his EIDL loan payments, but that still left him with the full loan.

"It was just surprising to me. You go into bankruptcy expecting to get most of your debt wiped out," Andelman said, adding that the EIDL funding was sold to him as a more owner-friendly option but, ultimately, it left him in the lurch. "The bank did threaten that they are going to go after me personally. So what's the benefit of the SBA loan if you are paying all those fees – for what?"

That means Andelman has to deal with substantial monthly payments to repay both the 7(a) lender and the SBA – which makes it impossible to scale back the business or shrink it down to a more manageable size. Business has begun to improve, and Andelman and his family have cut back on expenses like going out to dinner and attending sporting events. He said he sees other business owners struggling the same way as the consumer landscape has shifted under their feet, even as they are forced to carry forward SBA loans for decades.

Those payments – which are starting up again now that Andelman has exited bankruptcy – will serve as an anchor around his business in a way that he had never anticipated. While his high-interest debt is gone, it was the funding he sought as part of the pandemic relief that will be the bulk of the debt burden going forward.

"The bankruptcy basically got us back to before Covid in terms of our bills, which is great. But did it help the way I thought it would? The jury's still out," Andelman said. "We were given an option: Go out of business or struggle. And we chose struggle. And it's still a struggle. And it wasn't like this before."

SBA skyrockets among small-business bankruptcies
The SBA ultimately approved more than 4.1 million SBA EIDL loans across 2020, 2021 and 2022, according to numbers updated on Feb. 2.

The rush to get as many loans as possible out the door in 2020 was later flagged by the SBA's inspector general as being rife with potential fraud and underscored by loose lending standards. The agency began to charge off its EIDL loans, essentially declaring them in default and uncollectible, and the number of those loans is growing.

In 2021, the agency charged off \$21.5 million in EIDL loans. In 2022, that grew to \$198.2 million. Last year, the agency charged off an eye-popping \$52 billion in EIDL loans – about 17% of its portfolio.

That number is likely to continue to climb. The SBA inspector general estimated the amount of delinquent or past due loans of \$100,000 or less to be about \$62 billion as of March 2023. The SBA has since said about 1.3 million EIDL loans are either past due, delinquent, in liquidation or charged off.

The SBA now finds itself in a spot it has never been before – as the main

creditor to an ever-growing number of small businesses choosing bankruptcy.

The Playbook reviewed business-level bankruptcy data from nearly 21,000 businesses across the 45 markets served by The Business Journals network of publications, with more than 8,000 listing a major creditor in their bankruptcy – and the number of filings that list the SBA has skyrocketed.

In 2019, the SBA is named as the main creditor in just three bankruptcies, according to the data reviewed. By 2022, that had grown to 111; by 2023, it had more than doubled, to 253. That figure stands to be surpassed this year, as the SBA was listed as the main creditor in 72 bankruptcies through March 20 – less than one-quarter through the year.

While in absolute numbers the total number of bankruptcies is small, the volume has made the SBA the most-cited major creditor among the dataset compiled by The Business Journals. For context, in 2023, American Express Co. was the major creditor in 13 bankruptcies, and Bank of America Corp. was listed in 14.

Additionally, while the nature of the loans couldn't be specified – in addition to EIDL and 7(a) offerings, pre-pandemic numbers in particular could involve SBA disaster loans or other loan programs – it's clear the number of bankruptcies in which the SBA is the one holding the debt is on the rise.

That doesn't mean the SBA will begin seizing assets and carting off restaurant or retail equipment. But it does mean, as the pandemic continues to recede from the everyday impact it had, a growing number of businesses that managed to stay afloat during Covid will go under and find there is much less leeway associated with holding an SBA loan than they might have thought.

The agency itself is under heavy pressure to collect on every dollar it's owed, which leaves business owners on the hook. That could mean garnished tax refunds and being barred from federal programs.

Matt Coleman, vice president at Mercury Public Affairs and a former spokesperson for the SBA, said there are serious consequences for businesses defaulting on SBA loans.

While the SBA often will attempt to work with a borrower – such as through its hardship program that shrinks and caps EIDL payments for six months – it ultimately will refer that debt to the Treasury Department, which often adds a 30% penalty on debts it collects on.

"Benjamin Franklin said it right: There are only two things certain in life. And U.S. Treasury will collect on one of them, usually through their Treasury Offset Program administered by the Bureau of Fiscal Services," Coleman said. "Even if a borrower doesn't pay Treasury, they will get their money by garnishing your tax refunds, your wages, a grant or any income you may receive just to resolve your debt ... and Treasury could even go further and garnish part of your Social Security payments."

He said small-business owners should "think long and hard" before

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considering bankruptcy, though, as it too has big consequences, such as prohibiting them from obtaining another government loan for 10 years.

SBA outlines its actions

The SBA said in a statement to The Playbook there has been no change in how it handles SBA loans when a borrower files for bankruptcy; the agency acts like a creditor in accordance with the law. What actions it takes depends on factors such as the liability of the debtor, the collateral involved, the assets and the type of bankruptcy, the agency said in its response after being contacted by The Playbook multiple times for this story.

“When SBA is listed as a creditor in a bankruptcy filing, SBA receives notice. Where appropriate, SBA takes action based on the bankruptcy notice to comply with the automatic stay, such as stopping communications and collections,” the agency said. “If appropriate, SBA files a claim in the bankruptcy case and collects in the same manner as other creditors in the same class.”

The SBA said it may coordinate with U.S. attorneys offices and bankruptcy trustees to recoup and protect taxpayer funds.

The SBA has rolled out a number of programs and reprieves for small-business owners overwhelmed by their Covid EIDL loans. At first, business owners only had to begin repaying EIDL loans after 30 months. The agency then instituted several rounds of “hardship” deferments that capped payments. In early 2024, it announced a 60-day “goodwill” exception period for some loans during which the agency would not send delinquent loans to the IRS or Treasury Department for collections – although it did not defer the interest collecting on those loans.

The SBA has drawn heat in the past from lawmakers for saying it would not collect on PPP loans of less than \$100,000, and lawmakers have been concerned the agency also would not collect on smaller EIDL program loans. The agency said its PPP collection efforts yielded very little and, ultimately, it costs more to try and collect than to write off the loans.

The SBA inspector general also has pointed out in reports to Congress that up to 17% of all Covid EIDL and PPP funding is potentially fraudulent – specifically, more than \$136 billion in EIDL money and \$64 billion in PPP loans, representing more than 4 million loans total. The SBA has disputed the watchdog’s methodology and conclusions.

The SBA has said in statements to The Playbook all business owners are required to pay back their EIDL program funding. The agency also has said the update to its collections process – in which it would push to recover loans wherever possible – was based off a new analysis using updated and more mature datasets.

Small businesses saddled by debt

Despite a comparatively robust economy with low unemployment and significant growth, many small businesses are straining under the weight of debt taken on during the Covid-19 pandemic.

While about 28% of small businesses report they have no outstanding debt – roughly the same as the 29% that said the same in 2019 – about

39% of small-business owners reported having more than \$100,000 in debt last year. That’s a notable increase from the 31% that reported more than \$100,000 in debt in 2019, according to the 2024 Report on Employer Firms: Findings from the 2023 Small Business Credit Survey, published by the Federal Reserve in March.

A report by online credit-report provider Creditsafe found 58% of U.S. businesses it surveyed have increased their long-term debt in the past 12 months, while 17% said their ability to repay their debt has worsened in the past year. Another report by asset-management group Janus Henderson Investors found companies worldwide took on a record \$456 billion of new debt between 2022 and 2023, and S&P Global found corporate debt defaults increased by 80% in 2023 alone.

While bankruptcy filings are on the rise, they still are nowhere near the levels seen before the pandemic, although experts expect they will continue to increase over the coming years.

Bankruptcy filings of all types peaked at around 1.6 million in 2010, during the height of the Great Recession, and plateaued at around 774,000 annually in the years leading up to the pandemic. In the subsequent years, with a host of relief programs for individuals, families and businesses taking effect, the number of annual filings slid to about 388,000, according to data from the Administrative Office of the U.S. Courts on behalf of the Federal Judiciary. That number increased to about 453,000 last year, and experts expect it will continue to rise in the months and years to come.

Larger companies already are seeing a substantial surge in bankruptcy filings, according to data from S&P Global Market Intelligence, which tracked bankruptcies for public companies and for private companies with either public debt of more than \$2 million or with assets or liabilities above \$10 million. By that metric, bankruptcies hit 642 in 2023, the highest annual mark since 2010 and far above the 372 recorded in 2022.

Jonathan Carson, co-CEO of Stretto, which offers corporate restructuring and bankruptcy services, said businesses can discharge SBA loans in bankruptcy, but if they pledged collateral, that will be taken as part of a broader liquidation. That’s not to be confused with other government debts that cannot be discharged, such as taxes, or harder-to-discharge debts, such as student loans.

While cases vary individually, Carson said business owners overwhelmed by their debt should consider bankruptcy rather than letting their EIDL or SBA loans fall into delinquency.

“Bankruptcy is a much cleaner approach to managing liabilities on your balance sheet than ignoring your liabilities and hoping they go away,” Carson said. “The stigma attached to bankruptcy 25 years ago no longer remains.”

For Andelman, he wishes he would have declared bankruptcy sooner.

“I would have declared bankruptcy immediately after the Omicron wave if I had known it worked,” he said. “I think it would have been easier and I would have been in a much better position.”