Access Denied: Eliminating Barriers and Increasing Economic Opportunity for Justice-Involved Individuals

House Financial Services Committee, Subcommittee on Diversity & Inclusion

Statement of the Collateral Consequences Resource Center for the Hearing Record

September 24, 2021

The Collateral Consequences Resource, founded in 2014, is a nonprofit organization promoting public engagement on the myriad issues raised by the legal restrictions and societal stigma that burden people with a criminal record long after their case is closed. Our legal experts analyze the laws and practices related to criminal record relief on a national basis, consult in support of reform efforts, produce legal and policy research, and participate in court cases challenging collateral consequences.

Our flagship resource, the Restoration of Rights Project, provides frequently updated state-by-state and federal profiles addressing: (1) limits on the consideration of criminal records in employment, occupational licensing, and housing; (2) pardon, expungement, and other forms of record relief; and (3) loss and restoration of civil rights. We provide further insights into these topics through 50-state comparison charts, annual legislative reports, a national survey and report card, model legislation, and a federal legislative agenda. Our recent national review of fair chance housing laws, which highlighted New Jersey’s recent state-wide legislation limiting consideration of criminal record in housing decisions, documents the rise of these policies at the local and state level.

We appreciate the opportunity to submit this written statement for the record. We will focus on restrictions on eligibility for federal government-sponsored small business loans based on criminal history, restrictions that represent a critical barrier to economic opportunity for justice-impacted individuals.

Starting a small business is increasingly recognized as one pathway to opportunity for individuals with arrest or conviction history—particularly given the disadvantages they face in the labor market. An estimated 4% of small businesses in the United States have an owner with a conviction (1.5% have a felony conviction). Small businesses provide “a vital opportunity for those with a criminal record to contribute to society, to earn an honest profit, and to give back to others.” They also frequently employ people with a record and help reduce
A growing number of organizations and government programs are devoted to supporting individuals with a record in developing entrepreneurial skills, obtaining business employment, and building their own businesses. Yet many structural barriers remain, among them a series of federal regulations and policies that impose broad criminal history restrictions on access to government-sponsored business loans, notably by the U.S. Small Business Administration (SBA). A recent article illustrates the steep challenges faced by business owners with a criminal record by telling the stories of several entrepreneurs who were either denied an SBA loan or were discouraged from even trying for one because of a dated felony conviction. One of those entrepreneurs comments: “You might do five years, ten years, one year, but you pay for it until you’re in the grave.”

Last year, the SBA blocked hundreds of thousands of small businesses from obtaining Paycheck Protection Program and COVID-19 Economic Injury Disaster Loan funds by adopting shockingly extensive criminal history restrictions not required or even suggested by statute. The PPP restrictions impacted at a minimum 212,655 businesses with 343,198 employees, with disproportionate impacts on Black and Latino communities. When we began to publish resources about these restrictions shortly after the passage of the CARES Act, our servers crashed because of the level of public interest, requiring us to update our systems. Thousands of business owners emailed us, with a wide variety of records and types of businesses, desperate for help. We developed informational material for a large bipartisan group of organizations calling on the agency to revise its criminal history restrictions. Congress held hearings and considered legislation to eliminate most of the restrictions. Individuals and organizations brought litigation, with a federal judge finding that the SBA had acted unlawfully in failing to provide an explanation for its initial criminal history exclusions. Successive executive branch decisions rolled back most of these restrictions on COVID-19 relief.

In addition, the SBA continues to impose extensive criminal record-related restrictions in its general small business loan programs, frustrating lawful efforts by entrepreneurs and employees with criminal histories. Over the years, the agency has incrementally added more and more restrictions, without a statutory directive to do so or a clear policy justification. (A notable exception is the agency’s repeal of some restrictions on microloans in 2015.) Indeed, there is no empirical research we can identify that supports the use of criminal history as a measure of credit risk. In contrast, the other major source of federal support for small business, the U.S. Department of Agriculture, imposes only narrowly defined criminal history restrictions that are specifically required by statute. The SBA’s restrictions (and similar restrictions in some state business loan programs) are often buried in forms and regulations with no accompanying justification, and typically are subject to little scrutiny or public debate.
To illuminate these barriers, our organization recently launched a “Fair Chance Lending” project. We aim to show that—rather than broadly exclude individuals with a criminal history—officials should draw record-based restrictions as narrowly as feasible, facilitate access to resources, and celebrate entrepreneurial efforts, consistent with growing national support for reintegration and fair chances in civil society. To that end, we have already identified the following concerns about the SBA’s criminal history policies:

**The SBA’s criminal history restrictions are not provided by statute.** The Small Business Act allows but does not require the SBA to conduct a criminal background check of loan applicants, and no statute provides that the agency should treat criminal history as a measure of creditworthiness. The only statutory criminal history restriction on SBA loans that we can identify is a half-century old exclusion from 7(b) disaster loans of persons convicted in the year prior to application of a felony “during and in connection with a riot or civil disorder.”

**Many of the SBA’s criminal history restrictions are also not codified in regulation.** For example, the SBA adopted a series of frequently changing criminal history restrictions for COVID-19 EIDL loans that were either unannounced or only disclosed through FAQs published on the agency’s website. Another example is 7(a) and 504 loans, which are subject to a regulation with certain limited criminal history requirements, but to far more extensive criminal history restrictions through policy statements and application forms.

**The SBA’s criminal history restrictions are overbroad and lack specific justification.** The SBA has adopted a range of rules over time without clearly articulating their rationale, except under the general rubric of a “good character” requirement. Many specific policies are surprising. For example, the SBA requires the disclosure and consideration of expunged and sealed records. Uncharged arrests, dismissals, acquittals, and other non-conviction records can be disqualifying. Diversions are often treated as if they were convictions. Felony convictions can be disqualifying regardless of how old they are. Restrictions often apply to various persons associated with a business, including owners of 20% or more equity and employees managing day-to-day operations.

**The SBA’s criminal history restrictions have racially disparate impacts.** Studies have already been published indicating the SBA’s criminal history restrictions on the Paycheck Protection Program disproportionately impacted Black and Latino business owners. The SBA’s comparable criminal history restrictions in its general loan programs likely have similar effects, given the well-documented racial disparities in the instance of criminal records in general. The SBA makes little effort to justify its broad policy-based restrictions, which heightens their contrast with the
targeted statutory restrictions that apply to rural-focused lending programs administered by the USDA.37

Small businesses are the backbone of the American economy and a critical pathway to opportunity, including for justice-impacted individuals. We urge Congress to conduct oversight and advance policies that facilitate access to resources for small businesses and reduce criminal history restrictions in federally sponsored small business lending.

1 https://restoration.ccresourcecenter.org/.
3 https://ccresourcecenter.org/resources-2/resources-reports-and-studies/.
4 https://ccresourcecenter.org/the-many-roads-to-reintegration/.
5 https://ccresourcecenter.org/model-law-on-non-conviction-records/.
older than six months and involve either: a non-violent conviction or a misdemeanor conviction not involving a prison sentence, or a non-violent or misdemeanor conviction involving a prison sentence not to exceed one year. If the applicant is under a deferred prosecution agreement, the applicant must also disclose any arrests in the past six months.

The SBA has removed the prohibition on individuals associated with the business who have a criminal record being “of good character” as determined by the SBA. This means that the SBA can no longer refuse to make a business loan to an individual based on their criminal record, unless the individual is under a deferred prosecution agreement.

The SBA has also updated its regulations to include a new section that defines an “Associate” as an officer, director, significant owner, or key employee of the small business. This means that if an individual associated with the business has a criminal record, the SBA must determine whether the individual is “creditworthy.” See 13 C.F.R. § 120.10(2). Another regulation defines an “Associate” as an officer, director, or key employee of the small business. See 13 C.F.R. § 120.150.

The SBA has also updated its regulations to include a new definition of “character” as a factor in determining whether an applicant is “creditworthy.” See 13 C.F.R. § 120.110. This regulation states that “character” is a factor in determining whether an applicant is “creditworthy.” See Business Loan Programs, 61 FR 3226-3266. SBA regulations define an “Associate” in pertinent part as “An officer, director, owner of more than 20 percent of the equity, or key employee of the small business.” See 13 C.F.R. § 120.10(2).

Another regulation states that “character” is a factor in determining whether an applicant is “creditworthy.” See 13 C.F.R. § 120.110. This regulation makes a business ineligible for business loans if they have an “Associate” who is incarcerated, on probation or parole, or has been indicted for a felony or “crime of moral turpitude.” See Business Loan Programs, 61 FR 3226-3266. The SBA has elaborated on these regulations in Standard Operating Procedures (SOP). For example, an Aug. 1, 2008, SOP governing 7(a) and 504 loans added a requirement that “an individual with a deferred prosecution is treated as if the individual is on probation or parole.”

The Office of Financial Assistance, U.S. Small Business Administration, SOP 50-10(5) Lender and Development Company Loan Programs (Aug. 1, 2008). Beginning in January 1, 2014, the SBA adopted more far-reaching policies in its SOP governing 7(a) and 504 loans, which are similar to the current policies described in detail below. Compare Office of Financial Assistance, U.S. Small Business Administration, SOP 50-10(5) (F) Lender and Development Company Loan Programs (Jan. 1, 2014) with Office of Financial Assistance, U.S. Small Business Administration, SOP 50-10(6) Lender and Development Company Loan Programs (Oct. 1, 2020).

The current SBA policy statement governing general business loans (7(a) and 504) provides that specified individuals associated with the business must be “of good character,” as determined by the SBA (this includes any proprietor, general partner, officer, director, managing member of a limited liability company, owner of 20% or more of the equity of the Applicant, Trustor, or any person hired to manage day-to-day operations). Each of these persons must disclose and provide documentation about: (1) any arrests in the past six months; and (2) for any criminal offense (excluding minor vehicle violations), any convictions, guilty pleas, no contest pleas, or any placements on pretrial diversion or any form of parole or probation, at any time. All expunged and sealed records must be disclosed. If any person has not satisfied all sentencing conditions (which may include payment of court debt), the applicant is not eligible for a loan. A lender may proceed with a loan (assuming all other requirements are met) if all the documented criminal records are older than six months and involve either: a non-conviction or a misdemeanor conviction not involving a prison sentence.
involving a crime against a minor. However, if any person has: a prior felony conviction that was not reduced to a misdemeanor; a prior misdemeanor conviction for a crime against a minor; or, within the previous six months, either a misdemeanor conviction or charges filed, they are required to complete an FBI fingerprint background check and undergo an individualized character determination by the SBA—before a lender may process the loan. (It is not known how often lenders actually proceed with the FBI/SBA process at that point rather than simply deny the application; it is also not known how often the SBA finds that such a person meets the “good character” requirement in its policy statement). A person who receives an adverse character determination may request a reconsideration within six months of a decision and must include additional information or documentation. Factors that contribute to a favorable reconsideration include information that explains the circumstances of the offense, the passage of time during which the person has not committed additional offenses “and has generally led a responsible life and contributed to the community,” and any additional law enforcement or court documentation. See SBA SOP 50-10(6) (Oct. 1, 2020).

22 See 13 C.F.R. § 120.707 (“An Intermediary may also make Microloans to businesses with an Associate who is currently on probation or parole; provided, however, that the Associate is not on probation or parole for an offense involving fraud or dishonesty or, in the case of a childcare business, is not on probation or parole for an offense against children.”).

23 See Taja-Nia Y. Henderson, New Frontiers in Fair Lending: Confronting Lending Discrimination Against Ex-Offenders, 80 N.Y.U. L. Rev. 1237, 1260 (2005) (“Notably, neither the SBA nor the private banking industry has attempted to measure the relationship between criminal exposure and creditworthiness.”).

24 Record-related barriers covering USDA lending programs appear to be few and targeted, rooted in statutes, and triggered by specific offenses. See, e.g., 21 U.S.C. § 889 (conviction for planting, cultivation, growing, producing, harvesting, or storing a controlled substance triggers prohibition for that crop year and four succeeding crop years on access various USDA loan, grant, payment and contract programs); 7 C.F.R. § 718.6 (same); 7 U.S.C. § 2209j (permanent or 10-year debarment from USDA programs for fraud in connection with USDA programs); 2 C.F.R. § 417.865 (same). One of the USDA’s business loan programs, for example, the Business & Industry (B&I) Loan Guarantees program, which is similar to the SBA 7(a) program but targeted to rural businesses, does not appear to contain any additional criminal history restrictions except an optional bank “character” review that is not specifically linked to criminal record. See 7 C.F.R. § 5001.202 (“When applicable, a [lender’s] evaluation [of an applicant] may include the character of persons with management control or a 20 percent or more ownership interest in the borrower.”).

25 “Prior to the approval of any loan made pursuant to this subsection, or section 503 of the Small Business Investment Act of 1958 [15 U.S.C. 697], the Administrator may verify the applicant’s criminal background, or lack thereof, through the best available means, including, if possible, use of the National Crime Information Center computer system at the Federal Bureau of Investigation.” 15 U.S.C. § 636(a)(1)(B).

26 Cf. 13 C.F.R. § 120.150(a) (SBA regulation stating that it will consider “character” and “reputation” in determining if an applicant is “creditworthy”).

27 See Department of Housing and Urban Development (HUD) Act of 1968, P.L. 90-448 § 1106(e). In addition, the SBA, like every federal agency, is subject to government-wide provisions that can result in disqualification from federal loans and grants for a period of time based on specific types of criminal convictions.


29 See note 21.

30 See, e.g., SBA SOP 50-10(6), pp. 152-57 (Oct. 1, 2020) (“The Agency requires that every proprietor, general partner, officer . . . must be of good character”). The notable exception was after the SBA was sued for failing to provide a reason for its criminal history restrictions in the Paycheck
Protection Program, the SBA revised its rules and stated that the pared back rules were based on the risk that being incarcerated, facing felony charges, or having recently been placed on parole or probation could impact ability to pay or potential misuse of funds. See Defy Ventures, Inc. v. SBA, 469 F. Supp. 3d 459, 476 (2020) (summarizing June 24, 2020 Interim Final Rule).

31 See SBA SOP 50-10(6), pp. 152-57 (Oct. 1, 2020).
32 See id. at p. 154; see also Is SBA denying disaster relief based only on an arrest?, Collateral Consequences Res. Ctr. (May 6, 2020), https://ccresourcecenter.org/2020/05/06/is-sba-denying-disaster-relief-based-only-on-an-arrest/.
33 See, e.g., id.
34 See, e.g., SBA SOP 50-10(6), pp. 152-57 (Oct. 1, 2020).
35 See, e.g., id.
36 See Bushway, et al., Small Businesses, Criminal Histories, and The Paycheck Protection Program, supra note 9 at 8 ("Although we do not have complete data on race, we find that the original PPP restrictions differentially affected Black individuals. The nationwide data that we have in which the race of the owner is known suggest that 24 percent of the businesses affected by the original restrictions were owned by Black individuals. This percentage could be much higher if Black owners are overrepresented among owners who have a missing racial status in the records."); Finlay, et al., Criminal Disqualifications in the Paycheck Protection Program, supra note 14 at 6 ("There is a disparate impact of [PPP] criminal justice-based disqualification criteria by race, sex, and age, with Black and Hispanic men, younger men, and Black women experiencing higher than average exclusion from PPP eligibility due to higher rates of contact with the criminal justice system in each [of the seven state[s studied.]”).
37 See note 24.