

DISPELLING SOME SBA MYTHS

I had the pleasure to recently meet with the new SBA District Director, John Woosley, and was able to clarify some of the prevailing myths regarding the SBA and its loan-guarantee programs. Here are the most common questions asked by clients exploring SBA financing:

1. Does the SBA lend money?

No, the SBA is not a direct lender! However, it does guarantee up to 85% of the loans banks make to business borrowers for the acquisition of existing businesses (7-A Program), new equipment (504 Program) and/or commercial real estate (504 Program). These guarantees make the banks feel more secure in their lending practices, which translates into more money available for borrowers. In the 7-A Program, the SBA will guarantee 85% of a loan of \$150,000 or less, and 75% of a loan more than \$150,000, to as much as \$2 million. Under the 504 Program, it will guarantee 40% of the total financing and subordinate its position in loans as large as \$4 million. Many banks are reluctant to loan money for the purchase of a business or franchise without an SBA guarantee but commercial real estate loans are usually available through normal banking channels as well as SBA programs.

2. Can I borrow 100% of the money I need through an SBA program?

Not usually! Some equity participation is generally required on the part of the borrower to defray some of the lender's risk and show genuine commitment. That amount can vary from 10% to 50% for the 7-A Program, depending on the type of industry. 10% down is fairly standard for the 504 Program although it can go as high as 20% in special circumstances. Since the bank is at risk for between 15% and 50% of the loan amount, the borrower's financial statement and credit report will also play a major role in whether or not the bank will make the loan even with the SBA guarantee.

3. Can I obtain financing without putting up the whole down payment?

Yes, if the seller is willing to carry back a promissory note for the difference. Seller's are often reluctant to do this because their promissory note is subordinate to the bank's note. This means that in the event of a default, the bank has first claim on the borrower's collateral. If there is anything left over, it can go to the seller. Many banks require a seller's note to be in a "standby" position, which means the purchaser can't start paying on the seller's note until the bank deems the business is healthy enough to support the two payments. A few banks require some seller-financing to reduce their risk and to keep the seller involved in the success of the business. This is not an SBA requirement.

4. Can I secure an SBA-guaranteed loan if there is no collateral?

The SBA's loan approvals are based on cash flow (the ability of a business or piece of commercial real estate to service the debt), and not collateral. However, if there is collateral available, the SBA will place a lien on that collateral.

5. What are the typical terms and conditions for these loans?

Most 7-A loans are payable over seven years at a floating interest rate usually about 2.75% over the prime rate (currently at 8.25%). The 504 program, because it deals with commercial property, allows payments of up to 25 years on the SBA portion of the loan (up to 40% of the entire project cost). SBA loans are never subject to balloon payments.

6. Are there any SBA programs that provide funding for minorities?

Generally speaking, SBA lending programs are available to all groups on an equal basis. The SBA's Small Business Resource Guide provides detailed information on all of its programs. Information is also available on its web site, www.sba.gov. Another SBA mandate is to help small businesses obtain government contracts and those programs help members of both minority and socially-disadvantaged groups.

7. What is the preferred lender program (PLP)?

Certain banks have chosen to specialize in SBA lending programs and have loan officers trained to administer these programs. These banks go through a special certification program, and when successful, are named PLP lenders. I would advise would-be borrowers to look to PLP lenders because of their expertise. However, John was careful to point out that there are many factors a borrower needs to consider in selecting a lender.

8. How else does the SBA help small businesses?

In addition to its lending programs, the SBA has cooperative agreements with SCORE (Service Corps of Retired Executives – Counselors to America's Small Businesses), Small Business Development Centers (SBDCs), and Women's Business Centers (WESST Corp.). These SBA Resource Partners provide valuable advice to both existing entrepreneurs and wannabes. They can help with marketing ideas, leases, business plan development, budgeting and hosts of other business disciplines. SCORE volunteers and the SBDC staff provide one-on-one counseling FREE to the small business community. SBA works with the three SCORE Chapters, nineteen SBDCs and six WESST Corp. offices located throughout New Mexico, as well as with ACCION NM (a non-traditional lender), The Loan Fund and other small business resources to help the state's small business be successful