

## **The Small Business Administration: What is it and how can it help your business?**

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### **What is the Small Business Administration?**

The Small Business Administration (the “SBA”) is a federal agency that originated in the early part of the 20th century as a means for the federal government to assist Americans struggling with the Great Depression. It’s gone through some name changes over time but essentially it has the same mission today as it’s always had, which is to help Americans start, build and grow businesses. One of the primary means by which the SBA does this is by assisting in providing loans to businesses.

### **How does the SBA loan program differ from traditional loans?**

The SBA normally acts as the guarantor of loans which are made by a lender – the SBA generally does not loan money directly to the borrower. The lender loans the money to the borrower and the SBA gives a limited guaranty to the bank that the money will be paid back. Through the use of the guarantee structure the SBA can help provide financing to businesses that might not otherwise qualify for loans through traditional lending sources. But in order to be eligible to obtain an SBA-backed loan borrowers have to meet certain eligibility criteria, which vary depending on the type of loan.

### **What’s the role of the lender in the SBA process?**

Businesses still typically apply to a lender, not the SBA, for the loan. The lender works with the borrower and (if the lender is an SBA Preferred Lender) makes a decision about whether or not to make the loan. The lender works directly with the SBA to make sure that the loan will meet the SBA requirements.

### **What are the most common SBA loan programs?**

The two main loan programs offered by the SBA are called the 7(a) Loan Guaranty Program and the 504 Certified Development Company program. Some of the main characteristics are:

7(a) program characteristics:

- Provides for broad financing needs of small businesses. Loan funds can be used for working capital, inventory, purchase of a business, and other business purposes
- Loan amounts under 7(a) program are currently up to \$2 million
- Term of 7(a) loan is maximum of 25 years (for the acquisition of land/buildings) and up to 10 years for working capital or inventory loan
- Interest rate is directly negotiated between borrower and lender (but is subject to SBA maximums)

504 program characteristics:

- Unlike 7(a), the 504 program is just for “bricks and mortar” investments—purchase of real estate and fixed assets (such as long-term machinery and equipment)
- Loan amount can be up to \$4 million
- Interest rates are pegged to an increment above the current market – rates can be very favorable, particularly in a tight credit market
- Term of loan can be up to 20 years
- The assets that are purchased are used as collateral for the loan
- Principals of the business have to each sign a personal guaranty

**The SBA is set up to help small businesses – but what does “small” really mean?**

“Size” is one of the factors looked at by the SBA to determine if a business is eligible for one of its programs. Size eligibility is tied to the business’ industry and is based on either the number of employees in the business or the business’s 3-year average annual revenues. The SBA or the lender will have to assist in determining if the size eligibility is met. Suffice to say that you do not have to be a “Mom and Pop” business to qualify – depending on the industry the business can have hundreds of employees and millions of dollars in annual revenue and still qualify. (For instance, for most retail trade industries the criteria is \$7 million annual average revenue).

**In addition to size, what are some of the other eligibility criteria for getting one of these loans?**

The criteria for the 7(a) and 504 programs are different, but generally:

- The business must be operating in the United States or its possessions
- The SBA has to have assurance that the loan will be repaid
- The loan proceeds must meet the permitted uses for that type of loan

**What impact has President Obama’s focus on small businesses had on the SBA?**

The American Recovery and Reinvestment Act of 2009 made \$730 million in funds available to the SBA to be allocated among its programs. Because the SBA had great success in generating

loans from the original funds provided under the Recovery Act, \$305 million in additional funding has been allocated (including, most recently, \$80 million in April 2010). The SBA has used the funds to make program changes to stimulate lending and unfreeze credit markets; the SBA:

- Increased guaranties in 7(a) program to up to 90% of the loan amount
- Reduced or waived borrower fees relating to the 7(a) and 504 programs
- Expanded eligibility criteria so that more businesses would be able to obtain loans

### **What has been the impact of these changes?**

SBA 7(a) loans in the first quarter of 2010 more than doubled over the first quarter of 2009 (\$3.7 billion versus \$1.6 billion). Part of this increase reflects that people who have lost their jobs have decided to become entrepreneurs and start their own businesses with loans from the SBA.

As a local example, Carolina First Bank has revamped its SBA division to try and take advantage of SBA opportunities. Carolina First has become an SBA “Preferred Lender” so that they can streamline the loan process for potential borrowers and have hired 19 new employees to handle SBA loans.

### **Given the SBA programs available, who should be looking at the SBA for assistance?**

While 7(a) and 504 loans are the SBA’s main offerings, there are a number of other programs the SBA makes available, including loans for companies that are in financial distress and loans designed for startup companies. Practically any business that is looking to use borrowing (as opposed to equity investment) to obtain funds for their company may be able to benefit from one SBA program or another.

### **Where can more information be found about the SBA and its programs?**

Since the lender (not the SBA) typically makes or approves the loans, ultimately the lender will be the best source of information about the various SBA programs they can offer, but the SBA website is a good resource itself – [www.sba.gov](http://www.sba.gov).

*This memorandum is provided by The Wyche Law Firm for educational and informational purposes only and is not intended and should not be construed as legal advice. We will be pleased to discuss with you in more detail SBA or other commercial loans. Please contact any of the following attorneys in our firm or your personal contact within our firm for more information.*

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