



TYPES OF SBA LOANS

The mission of the U.S. Small Business Administration (the “SBA”) is to promote small business success in America. One of the ways the Agency does this is by offering loan programs which increase access to capital. The SBA has two major loan programs: the “7a” and the “504”. Information on each of these programs and the process for obtaining each type of loan is described below.

SBA 7a Loans

The purpose of the 7a loan program is to assist for-profit small businesses obtain a loan for most legitimate business purposes. Under this program, the SBA guarantees a portion (50% for example) of a loan made by a lender, typically a bank. This makes approval of a loan application more likely. After the lender approves the loan, it then applies to the SBA for a guarantee. If the SBA agrees to guarantee the loan, the lender funds and manages the loan just like its non-SBA loans. In most cases, the small business owner never talks to the SBA. He/she applies for a loan with a lender just like any other business loan. It is then up to the lender whether to apply for a SBA guarantee.

Besides making approval more likely, the 7a program allows lenders to offer terms that are normally not available without a SBA guarantee. Specifically, lenders may offer a longer loan life and a lower down payment when they obtain a SBA guarantee. As compared to a non-SBA loan, this means lower loan payments and a smaller up-front investment when a business is purchasing real estate, equipment, or acquiring another business. Although SBA programs allow lenders to offer more favorable terms, it is the bank’s decision how to structure its SBA loans. To better prepare for a meeting with a lender, it is a good idea to visit a local SCORE office to discuss how a SBA guarantee might improve the chances of approval and the loan structure.

SBA 504 Loans

Under the 504 program, the for-profit small businesses get a loan that is funded by the SBA but handled by a Certified Development Company (a “CDC”). This loan is subordinated to a loan from a lender, thereby making the lender’s loan less risky. Like the 7a program, this makes bank approval more likely. Unlike the 7a, the 504 program does require new job creation or some other public purpose, such as helping a veteran or woman owned business. Another difference is that the 504 may be used to finance only owner-occupied real estate projects or equipment with a useful life of at least ten years.

If a small business wants a 504 loan, the owner will need to obtain approvals from a bank as well as a CDC. It does not matter which lender is contacted first. The CDC application process is just like a bank’s application but with a few more pieces of paper. The role of the local SBA

office on 504 loans is mostly educational. The CDC staff will guide a borrower through the application process and assist the borrower with the SBA application.

The typical structure of a 504 loan requires the borrower to have a 10% down payment. Most bank loans to purchase real estate require at least 20% down. The bank's first mortgage typically finances 50% of the cost of the project and the SBA/CDC loan usually covers 40%.

Besides making bank approval more likely, there are two other advantages a borrower gets when using the 504 program. The SBA/CDC loan is almost always lower than the rate on the bank's first mortgage loan and is fixed for as much as 25 years. This eliminates the risk that the interest rate might increase over the life of the loan.

Eligibility

Most small businesses are eligible to use SBA loan programs, but some are not depending on factors such as:

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| Size | In order to use a SBA loan program, the business must be "small" as defined by the SBA. To be considered small by the SBA, the borrowing company and all related companies must have a combined net worth of less than \$15 million and average net income of less than \$5 million over the last two years. |
| Industry | Some industries may not use a SBA program. For example, no business that promotes a specific religion is eligible. A business involving gambling is another example of an ineligible business. |

Eligibility can be a complex issue, so please visit sba.gov/programs for a detailed discussion of this topic.

Loan Size

The maximum size of any single SBA loan is typically \$5 million, although this may go to \$5.5 million in some cases. There is no limit on how many SBA loans a company, or group of related companies, may have. Rather, there is a limit on the total amount which the SBA will guarantee for any single group of related companies under the 7a program. This limit is \$3.75 million. The SBA does not impose a minimum loan size, but some lenders do. The limit on SBA 504 loans is typically \$5 million.

SCORE Mentors can assist you with the SBA loan process. To request a Mentor visit the SCORE website at scoreworks.org and register. You will be assigned a Mentor who will contact you and provide guidance through the SBA loan process. You can also contact the SBA directly 513-684-2814 or go to sba.gov for more information on the Agency's products and services.

If you would like to request a Cincinnati SCORE counselor please [click here](#).

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