The Myths and Realities of SBA Loans

With the economy recovering, now is a good time for businesses to secure financing. When a company has the proper capital in place, it can seize growth opportunities and expand to stay a step ahead of the competition.

When you think about capital, the SBA is a key resource to consider. Its loans are available through banks and can provide an essential resource at the right time. Dave Jackson, vice president and national SBA director at Fifth Third Bank, shares an overview here. Read it to learn how SBA financing may be able to help you.

Understanding the SBA

The U.S. Small Business Administration (SBA) began backing loans to businesses in 1954 to help American businesses expand, create jobs and reinvest their profits. Fifth Third Bank has been a preferred SBA lender for a quarter century. Currently, the agency sponsors eight government-guaranteed loan programs along with a collection of state offerings. During the recent recession, SBA-guaranteed loans were extended to midsized businesses as well as smaller companies. “Most of our SBA clients have revenues of $20 million or less, but we also look at companies with up to $70 million in revenues,” Jackson explains. “There are very few limitations on business eligibility.”

How SBA loans work

Along with being government-guaranteed, SBA loans carry other benefits. For example, banks accept lower down payments on SBA-backed loans — typically 10 percent rather than 20 percent. SBA loans also carry longer terms — 25 years rather than 20 years — which results in lower monthly payments for a business. Both fixed and variable interest rates are also capped on SBA loans. “The interest rates vary a little but they are typically very reasonable and may be lower than what business owners would pay with non-SBA or non-bank lending,” Jackson says.

Myths and misconceptions

Some business owners shy away from SBA loans because they fear that a government regulator will audit their business if they apply for a loan. “That’s not true,” Jackson explains. “The government never interferes with the loans.”

On the other hand, Jackson also explained that he encounters business owners who believe that the SBA will guarantee their loans even if they are not creditworthy. “Also not true,” he explains. “You have to have the cash flow to make the payments. The government won’t guarantee a risky loan — regardless of the collateral you put up.”

Popular programs

For businesses that need capital to bolster cash flow, fill new orders and fund growth, the most commonly used SBA program is the 7(a) loan. A bank can lend up to $5 million under this program and up to $350,000 under its 7(a) Express loan, which involves less paperwork. Another popular use of SBA loans is a making a real estate purchase via the SBA’s 504 loan program. With the 504 loan, property is the collateral. While it’s the bank that underwrites and funds these SBA loans, the government guarantees the loans. This guarantee makes riskier, smaller loans attractive to banks because it reduces their potential losses.

Required guarantees

Borrowers who own 20 percent or more of a company that is applying for an SBA loan must sign personal guarantees of repayment. “If no one owns 20 percent, at least one owner must step up and personally guarantee the loan. That requirement is mandatory,” Jackson explains. Before applying for a loan, he recommends that a business owner seek out an accountant to put together solid financial reports on the business, update its business plan and compile a customer list with repayment history. All this information will support the company’s application by showing its ability to repay the loan in a timely and consistent fashion.