Finance Primer: A Guide to SBA's Loan Guaranty Programs

Text File

Slide 1 Finance Primer: A Guide to SBA's Loan Guaranty Programs

Welcome to SBA's online training program, the Finance Primer: A Guide to SBA's Loan Guaranty Programs.
This course is a product of the agency's Small Business Training Network and is championed by the Office of Entrepreneurial Development.

Slide 2 Introduction

This is a self-paced training program about financing a small business and SBA's loan guaranty programs.
It is a practical course with real-world examples and helpful tips.
The course is directed to small firms who are interested in borrowing money.
You will find the course easy to follow and the subject matter indexed for quick reference and easy access. It will take about 30 minutes to complete the training program. Additional time will be needed to review included resource materials and to complete the suggested next steps at the end of the course.
The outlined "next steps" at the conclusion of the program are an integral component of the course.
They will help you apply what you have learned.
When you complete the course, you will have the option of receiving a printed Certificate of Completion from the SBA.

Click the forward button below to get started.

Slide 3 Course Objectives

This course has four key objectives:
1. Identify sources of capital most frequently used by small businesses.
2. Review basic finance principles.
3. Identify and describe SBA's loan guaranty programs. And,
4. Provide practical guidance and direct links to additional information and resources that can assist you in financing your business.

Slide 4 Course Outline

There are six topic sections within the course. Each section covers a different aspect of borrowing money and SBA's loan guaranty programs.
Reviewed together the topics weave a helpful platform that will assist you in raising money for your business.

Slide 5 Course Outline

This is not the type of training program you want to review once and put aside. It is a guide with many opportunities for the viewer to access more detailed information, especially about SBA's loan programs.

You will notice a button in the top right section of each slide that says Course Outline. Clicking on that button will bring you to the course outline – which will give you quick access to any section of the course.

Let's get started………

Slide 6 Key Sources of Capital

Financing your business or raising capital is the most basic of all business activities.
It is important to explore all sources before making a decision.
The primary source of funding for most new businesses comes from the owner's savings and other personal resources.
In addition, many entrepreneurs look to private sources such as friends and family when starting out in a business venture. Often, money is loaned interest-free or at a low interest rate, which can be beneficial when getting started.
However, funding for business growth or expansion most commonly comes from banks and non-bank lenders. They will provide financing if you can demonstrate an ability to remain in business, ability to repay the loan and meet the firm's other obligations.
Another source of capital, but one that is more difficult for new small businesses, is funding from angel investors and venture capital firms. These individuals and firms help expanding companies grow in exchange for equity or partial ownership.

Slide 7 Borrowing Money

As the focus of this course is **finance**, ---- let's assume you made the decision to borrow money for your business.
There are several things you should know upfront.

First. There is no such thing as 100% financing. You will be required to put money into the business, before a lender will provide financing.
Second. There is no such thing as a government grant for individual small businesses. Contrary to what some unscrupulous sales pitches will suggest, there are no government sources, including the SBA, that provide free money for opening or growing a for-profit small business. If it sounds too good to be true, it probably is.
Third. SBA does not lend money directly to small businesses, for any purpose, other than disaster assistance. Rather, SBA is a guarantor. It guarantees loans made by lenders to small firms. SBA provides a level of security to lenders, so they will provide financing to small businesses who might otherwise not be able to obtain financing from a lender.
Fourth. Your credit history is important! Get a copy of your credit report and review it. If there are any credit issues that can be remedied, before meeting with a lender, do so. A lender may be able to make exceptions if you can document that a negative credit report was due to circumstances beyond your control. If this applies, include a detailed written explanation with supporting information in your loan package.
And lastly, A lender will probably ask for a personal guarantee, even if you are incorporated. It is unlikely this can be avoided.

Slide 8 Borrowing Money (cont)

While the process of getting a loan can be time consuming and even frustrating, your chances of being successful are greatly increased, if you are informed and well prepared.
Being informed.., means doing your homework and understanding the borrowing process. ---- Being prepared.., means preparing responses to and addressing the most common questions a lender will ask. Questions such as: - What is the specific purpose of the loan? - How much of a loan are you requesting? - When and how long will you need the funds? - How will the loan be repaid? - What collateral can be used to secure the loan? - and, Will you provide a personal guarantee?
Answers to these questions, as well as supporting documentation are essential to the lending decision and will shape your lender's response. Typically --- these questions would be addressed in an interview with a banker or in a loan request package prepared for a lender.

Slide 9 Borrowing Money (cont)

In the spirit of sound preparation….., one of the most important things you should do is to prepare a written loan request package or proposal. This assumes you already have a business plan. If you do not, you need to prepare one.
A good loan package should tell a compelling story and answer most, if not all questions, a lender may have about your business and loan request. It will provide enough information and documentation so that your loan request is clearly understood and that your lender could discuss and defend it before a loan committee. Loan packaging is not an exact science. There are three major components of a loan package, with some components containing multiple parts. Again, this is not an exact science and different lenders require different things. However, for our discussion and general purposes, we will focus on the following components: statement of purpose, business plan and financial statements.
The statement of purpose is sometimes developed within a letter to a specific lender or is otherwise labeled the "executive summary" and is attached to the business plan.
How it is done is up to you….. What's important is that it be well written and informative, as it will likely be the first thing the lender reviews. It should include information about the request in terms of amount, purpose, duration, repayment and available collateral. It also should include a brief description about the business and include a crisp narrative outlining the positive effects the loan will have on the business.
Having a comprehensive, well thought-out business plan is essential to the financing process. You need a business plan before a lender will provide a loan. In fact, without one, even approaching a lender may be pointless.
Financial statements are also a critical and necessary component of a loan request package. They tell a story about the financial capacity and performance of a business. A well prepared loan proposal will include four types of financial statements: cash flow statement; income statement; balance sheet and personal financial statement.
Preparing a solid loan request proposal is more than just important. When you are ready to prepare such a proposal, and at your convenience, click on the hyperlink to review a comprehensive training module on how to prepare a loan package.

Slide 10 Borrowing Money (cont)

After you submit your loan request to a lender, how will it be evaluated?

Your lender will review your request using three key credit factors. But first, its important to point out -- that lenders are in the business to make money and the way they make money is by making loans. However, a loan officer's career is based on not making mistakes.

The bottom line…… you have to convince the lender that you and your business are a good risk. Your character, capacity and collateral, among other credit factors, will be considered by the lender in making a loan decision.

•Character is actually a check on your financial status and personal credit history, including your previous loan payment record. The theory is -- people are creatures of habit – if you have repaid prior debts on time and in full, you will likely pay this requested loan on time. Also considered is experience in the type of business you are trying to finance, including level of responsibility, education and business management training.
•Financial capacity is about having sufficient cash flow to pay-off a loan. This underlies the importance of preparing a cash flow statement with future cash projections before presenting your loan request to a lender. Doing so indicates that you are knowledgeable about the cash coming into your business and being spent. In the lender's mind, it shows that you are "financially aware" and that you may be better able to avoid a cash shortage that would jeopardize making monthly loan payments.
•Lastly, while cash flow is the primary source of loan repayment, lenders will want a back-up or secondary source, as an "exit of last resort," should your business not prove profitable. Collateral is that secondary source and it is important to the lender because it lowers risk. Remember, its all about lowering risk so the lender feels confident the loan will be paid on time and in full.

Slide 11 Borrowing Money (cont)

Suppose you had an opportunity to ask a banker, how to best prepare for getting a loan. What advise would you get?
You would likely be told……
*Be prepared. Know how much you need to borrow and how the funds will be specifically used.
*Know your options. Learn what loan programs are available and discuss your options with knowledgeable people.
*Prepare a written loan request package, as we just discussed and make certain it includes a business plan with current financial statements. Whatever you prepare, it should be brief, to the point and easy to read. It should emphasize the management strength of your business, convincing the lender that you and your team have the skills, passion and expertise to be successful.
*Proofread what you prepare. Better yet, have someone else go through it for spelling, grammar and style.
*And finally, learn from your mistakes. If you get rejected from one lender, find out why and FIX the problem.

Slide 12 SBA's Loan Guaranty Programs
We have talked about the borrowing process and how to prepare yourself for a loan. Now, let's review SBA's loan programs.
The agency administers several loan programs. Through these popular initiatives, loans are made by private lenders to small firms with a guaranty by the SBA.

The guaranty transfers the risk of the borrower, up to the amount of the guaranty, from the lender to the SBA. As such, when a business applies for an SBA loan, it is actually applying for a commercial loan, structured to SBA's requirements and receiving an SBA guaranty.
SBA loans have helped thousands of small businesses. These loans offer longer terms than typical commercial loans, which generally mean lower monthly payments at competitive interest rates.
SBA guarantees over $10 billion in business loans each year. The agency's financial programs make a significant difference. ---- First for the individual firms who receive assistance, and second for the economy, because they spark investment, growth and the creation of new jobs.
The agency offers four distinct loan programs.
* The basic 7(a) loan program which is its biggest financial assistance program.
* Special purpose loans – which use 7(a) authority to create targeted loan programs.
*The micro-loan program.
*And, the certified development company – 504 program.

Each of these programs will be discussed in the following sections.

Slide 13 7(a) Loan Program

7(a) loans are the most basic and most popular of SBA's business loan guaranty programs. The name comes from section 7(a) of the Small Business Act, which authorizes the Agency to provide business loans to America's small businesses. **More than 80 percent** of all business loans guaranteed by the SBA are made under the 7(a) program.
7(a) loans are only available on a guaranty basis. This means they are provided by lenders who choose to structure their own loans by SBA's requirements and who apply and receive a guaranty from SBA on a portion of the loan. The SBA does not fully guaranty these loans. The lender and the SBA share the risk, if a borrower is unable to repay the loan in full.
All 7(a) loans are provided by lenders, called "participants" because they participate with SBA in the program. Not all lenders choose to participate, but many banks and non-bank lenders around the country do.
Under the guaranty concept, commercial lenders make and administer the loans. If a payment default occurs, the Government will reimburse the lender for its loss, up to the percentage of SBA's guaranty. A typical guaranty percentage will be in the 50 to 75 percent range, depending on the type of loan and other factors. Some special purpose loans, which we will discuss later, may carry a higher guaranty percentage.
Lenders generally seek an SBA guaranty after they have evaluated the credit merits of an application and determined that additional support is needed.

Through its guaranty, SBA is able to assist tens of thousands of businesses each year to obtain financing that would otherwise not be available.

Slide 14 7(a) Loan Program

To be eligible for a 7(a) loan guaranty, several general requirements apply. These are in addition to credit and repayment standards discussed earlier.
General requirements include specific size standards, type of business and purpose of the requested loan. Each of these eligibility requirements is discussed in the following sections.

Slide 15 7(a) Loan Program

Certain government programs only apply to small businesses. To qualify for SBA's financial assistance programs, you must meet specific small business size standards.
Over the years, SBA has established and revised numerical definitions for all for profit industries, and this numerical definition is called a "size standard." It is almost always stated either as the number of employees or average annual receipts of a business concern.
To participate in SBA's loan guaranty programs, you must meet the agency's small business size standards. In general, a business is considered small if it is independently owned and operated, is not dominant in its field and meets the size standards applicable to its specific industry. Generally, the size standards are as follows:
As a wholesale business, you can not have more than 100 employees.
As a retail or service business your annual revenue can not exceed $21 million.
A manufacturing firm generally can not exceed 500 employees.
And, if you operate as a construction firm, average annual sales can not exceed $17.5 million.

To learn more about size standards, click on the hyperlink.

Slide 16 7(a) Loan Program

SBA can and does provide financial assistance to most types of small firms.
However, assistance can not be provided to: non-profit organizations or businesses engaged in financing real estate for investment. Also, SBA can not provide financial assistance to firms involved in illegal activities or firms that conduct gambling, speculation, lending or investment activities.
And finally, SBA will not support a monopoly situation or businesses engaged in pyramid sales.

Slide 17 7(a) Loan Program

SBA guaranteed loans can and are used for many purposes. In general, SBA will support the financing of a new business start-up, the acquisition of an existing business and/or business expansion and growth. Specific loan purposes may include: purchasing land or buildings; acquiring equipment, machinery, or other business materials; working capital requirements; purchasing an existing business or refinancing existing business indebtedness -- that is not already structured with reasonable terms.

Slide 18 7(a) Loan Program

In addition to good credit and eligibility criteria, an applicant should be aware of the general types of terms and conditions they can expect if SBA is involved in the financial assistance. The specific terms of SBA guaranteed loans are negotiated between an applicant and the participating financial institution, subject to SBA's requirements. This is an important point. Again, specific terms of SBA loans are negotiated with the lender.
In general, provisions regarding loan maturity, interest rates, and the SBA guaranty are standardized and apply to all SBA 7(a) loans. There are some exceptions, specifically regarding special purpose loans, and they are discussed later in the course.
Each of the identified provisions is explained in the following sections.

Slide 19 7(a) Loan Program

The actual loan term or maturity will vary according to the economic life of the assets being financed and the applicant's ability to repay. However, there are maximum terms that will be applied. For working capital loans the maximum maturity may be up to 10 years; for machinery & equipment loans the maturity may be up to 25 years; and for real estate or business purchase loans the maximum maturity may not exceed 25 years.
Loan maturity is a function of a business's ability to repay. All loans supported by the SBA will be structured for repayment over the shortest possible time period, without causing undue hardship to the cash flow of the business.

Slide 20 7(a) Loan Program

Loan interest rates are negotiated with the lender. Generally speaking, many SBA loans have a variable rate tied to the prime rate, although some may have a fixed interest rate.
However, these rates cannot exceed SBA maximums of up to 2.25 percent over prime for loans of less than seven years, and up to 2.75 percent over prime for loans of seven years or longer.
Loans of $50,000 or less may be subject to slightly higher rates in order to induce lenders to make these smaller loans.
In summary, interest rates for guaranteed loans reflect prevailing market rates and can either be fixed over the life of the loan or can fluctuate with the market.

Slide 21 7(a) Loan Program

SBA provides its guaranty on only a portion of the total financing provided by the lender, not the entire amount. As a result, there is a lender share and an SBA share of each loan. The SBA share is also known as the guaranteed portion.
The maximum guaranty percentage is 75%, except for loans under $150,000, which may receive an 85% guaranty. However, not to confuse you, but Export Working Capital loans may receive a 90% guaranty.
The maximum share of SBA’s guaranty exposure for any one business is $1,500,000.

Slide 22 7(a) Loan Program

When an SBA loan guaranty is approved, the participating lender must pay SBA a guaranty fee.
This fee can be, and almost always is, passed on to the borrower.
The fee is based on the maturity of the loan and the amount of the SBA share.
Specifically, for loans with a maturity of 12 months or less, the fee is 1/4 of one percent of the guaranteed portion of the loan.
For loans with a maturity exceeding 12 months, the fee is: 2.0% on loans of $150,000 or less; 3.0% on loans from $150,001 to $700,000; or 3.5% on loans over $700,000.

Slide 23 7(a) Loan Program

Ok – we have covered a lot of ground. By now you know that the SBA 7(a) loan guaranty program is a key vehicle for providing financial assistance to small firms. You also know that SBA is a guarantor and that actual loans are provided by private lenders.
Over the years, many types of 7(a) loans have been born, but they are all program variations operating within the agency’s statutory 7(a) loan guaranty authority. Is goes without saying that SBA’s loan

programs are meant for small businesses. However, it is important to point out that some of SBA's loan programs are designed to support specific and targeted small business needs and others are designed to support the processing needs of lenders who ultimately are responsible for delivering the loans to our mutual small business customers.

Having said that, in addition to the basic 7(a) loan program, SBA features Patriot Express, SBA Express and Community Express, all variations on the basic 7(a) loan guaranty program. Each of these targeted variations support different market needs. Click on the hyperlinks to learn more about the different types of 7(a) loans.
Not to confuse, but to inform you, SBA also operates other programs for lenders to facilitate the efficient and effective delivery of 7(a) loans. These programs include the Certified Lenders Program, CLP, the Preferred Lender Program, PLP and the Secondary Market Programs. These lender programs are mentioned for your information only.

The BOTTOM LINE --- educate yourself on SBA's programs, but discuss your options with a qualified lender to get the best financing for your business.

Slide 24 Special Purpose Loans

As referenced earlier, SBA offers various special purpose loans that serve specific markets. These financing options use the agency's basic 7(a) loan authority, but offer differing guaranty levels and other variations to reach specific markets.
Special purpose loans currently support export markets and are also available to help employees buy ownership stock in a business or provide financial assistance to firms negatively impacted by NAFTA. Special purpose loans are designed to be short-lived programs that exist only during times of market need.

To learn more about specific special purpose loans, click on the hyperlinks.

Slide 25 Micro-Loan Program

In addition to the 7(a) loan guaranty program and special purpose loans, SBA offers micro-loans.
The Micro loan Program is designed to provide very small loans to small business clients who have had difficulty obtaining conventional financing for small amounts.
These loans are provided exclusively by approved intermediaries – typically nonprofit or economic development organizations.
Under this program, SBA makes or guarantees loans to intermediaries, who use the money to make micro-loans to eligible borrowers. Through this program, the SBA helps fill the very small loan financing gap created by the absence of traditional lenders providing smaller sized conventional loans.
The average size of a micro-loan is about $13,000. The maximum size of a microloan can be $35,000.
Micro-loans are available only to borrowers who can demonstrate they are unable to obtain credit elsewhere at comparable interest rates and who have good prospects for repayment.
Click on the hyperlink to learn more about micro-loans.

Slide 26 Certified Development Company 504 Program

Finally, in addition to 7(a), special purpose and micro-loans, SBA offers the 504 program.

The 504 program is an economic development financing program designed to stimulate private sector investment in long-term fixed assets -- which will increase productivity, create new jobs, and increase the local tax base. This program is administered through SBA-Certified Development Companies and requires at least a 10 percent contribution from either the CDC or the borrower. A higher contribution is required by law for start up businesses or when a unique or single purpose building will serve as the primary collateral. Additional borrower contribution can also be required as a matter of credit.
The 504 loan program also has a jobs requirement. The borrower must show that they will either create or retain at least one job for every $35,000 of financing support provided by the 504 program.

Click on the hyperlink to learn more about the 504 program.

Slide 27 Next Steps

Much material has been shared and we have certainly covered a lot of ground.
The instructional part of the program is complete. It is now up to you to apply what you have learned. This is the most important part of the course. If you are serious about seeking SBA financing support, consider following the next steps.

Step1. Estimate your business start-up costs or funds needed to grow your business.
Step2. Visit or call a local bank or lender to review available small business loan programs
Step3. Prepare a draft loan proposal.
Step4. Discuss what you learned from this course and steps 1, 2 and 3 above with a business mentor, coach, lender or SBA representative.

Slide 28 Additional Assistance

Many resources are available to assist you. The following resources can help you build a foundation of knowledge.
•SBA has over 60 district offices located throughout the country to help you start and grow your business. They can also help you find a lender to structure an SBA loan.
•There are more than **1,000 Small Business Development Center** locations around the country. **SBDC's** provide management assistance to current and prospective small business owners.
•SCORE is a powerful source of free and confidential small business advice to help build your business. More than 10,000 SCORE volunteers are available to share their wisdom and lessons learned in business.
•The Small Business Training Network is a powerful virtual campus.
•And finally, **Women's Business Centers** assist women in achieving their dream.
Some 90 WBCs are located around the country.
Click on these resources to learn more and access their assistance.

Slide 29 Other Resources

Other specific and very helpful resources include:
SBA's financing information section on the Web; SBDC-Net; a free online business planning course; SCORE's business tools and templates; and an agency checklist of required documents for SBA loan guarantees.

Slide 30 SBA Financing Forms

Additional resources to support the preparation of a loan request include a menu of SBA financing forms.
These SBA forms include a business loan application; schedule of collateral; balance sheet; income statement; cash flow statement and a personal financial statement.

Slide 31 Have a Question?

Never let a question go unanswered.
This course has covered a great deal of material. And, there is much to learn and understand about finance and SBA loan programs. If you have questions about any of the topics highlighted in this course, contact SBA or one of our resource partners.
We will help you.
Use the 800 number or referenced hyperlinks to contact us directly.

Slide 32 Course Completion Certificate

CONGRATULATIONS ON COMPLETING THIS COURSE.
WE HOPE IT WAS HELPFUL AND PROVIDED A GOOD WORKING
KNOWLEDGE OF NEW TECHNOLOGIES CAN BENEFIT SMALL BUSINESSES.
YOU EARNED A CERTIFICATE OF COMPLETION FROM THE SBA.
THANK YOU FOR PARTICIPATING IN THIS COURSE. WE WISH YOU THE VERY BEST IN THE FUTURE. CLICK THE PRINT BUTTON TO RECEIVE YOUR CERTIFICATE.