

Introduction to SBA 7a Lending

Mid America Lenders Conference

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Types of Guaranteed Loans

▶ SBA 7 (a)

▶ SBA 504

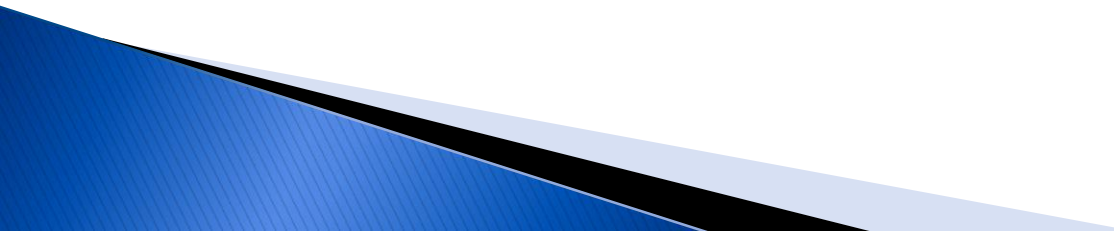
▶ USDA

SBA 7(a)

- ▶ The backbone of the U.S. Government Guaranteed Loan Programs to small businesses.
- ▶ Guarantees from 50%, 75%, 85% or even up to 90% depending on the delivery method.
- ▶ Legislative limit of \$5 million for the total loan and \$3.75 million for the total guaranteed portion.
- ▶ Loans made for business use, including financing of inventory or accounts receivable, business expansion, acquisition of a business, purchase of machinery and equipment, and purchase or refinancing of commercial real estate.

SBA 7(a) Eligibility

To be eligible the Applicant business must:

- ▶ Be an operating business (or will become operational with loan proceeds)
 - ▶ Be a for-profit entity.
 - ▶ Be “small”.
 - ▶ Be located in the U.S.
 - ▶ Demonstrate a need for the desired credit.
 - ▶ Not be listed as an ineligible type (§120.110)
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Ineligible Business Types (13 CFR §120.110)

- ▶ Passive businesses (i.e.: landlords, RE developers).
- ▶ Life insurance companies (Agents may be eligible).
- ▶ Pyramid Sales Distribution Plans.
- ▶ Gambling.
- ▶ Prurient Nature.
- ▶ Private businesses that restrict patronage.
- ▶ Government-owned businesses.
- ▶ Religious businesses.

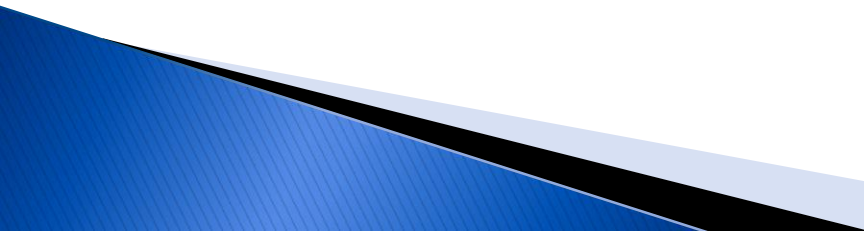
Ineligible Business Types (Cont.)

- ▶ Financial businesses (engaged in lending).
- ▶ Non-profits
- ▶ SBA Loan Packagers.
- ▶ Businesses in which the Lender has an equity interest.
- ▶ Illegal activity.
- ▶ Prior loss or Delinquent Federal debt.
- ▶ Political lobbyists.
- ▶ Speculative businesses.

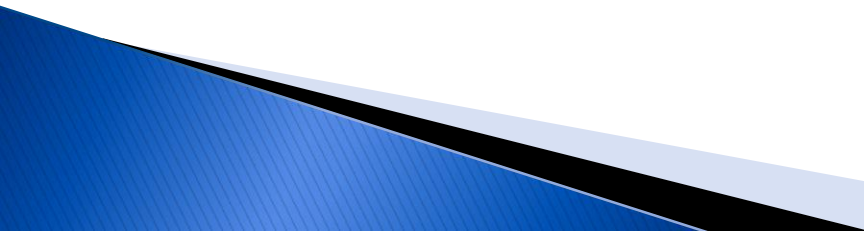
Other Eligibility Factors

- ▶ In the case of real estate, the property must be at least 51% occupied by the borrower; unless it is a new construction project, in which case the property must immediately be 60% occupied by the owner with plans to expand into 80% within 3 years and occupy 80% in 10 years.
- ▶ Cannot re-lend proceeds.
- ▶ Cannot benefit an ineligible affiliate.


SBA 7(a) Maturities

- ▶ Loans made for working capital or business acquisition carry maturities of 7 to 10 years.
 - ▶ Machinery and equipment loans have maturities of 10 years or the useful life.
 - ▶ Real estate loans have 25 year maturities.
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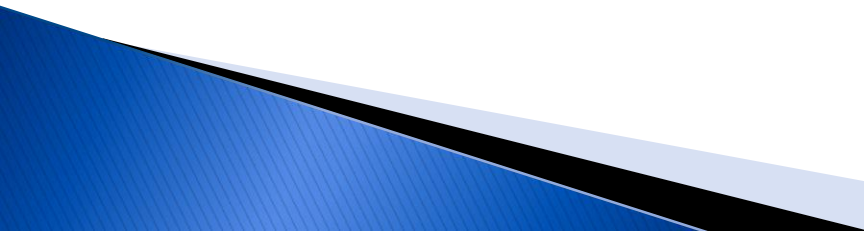
SBA 7(a) Maturities (Cont.)

- ▶ Where there are multiple uses of proceeds, a weighted average maturity can be used, or, maturity can be determined by the asset class of which the majority of loan proceeds have been allocated.
 - ▶ The loans are amortized with even payments and typically carry variable interest rates based on the Prime Rate plus some percent up to 2.75%, adjusted on a monthly or quarterly basis.
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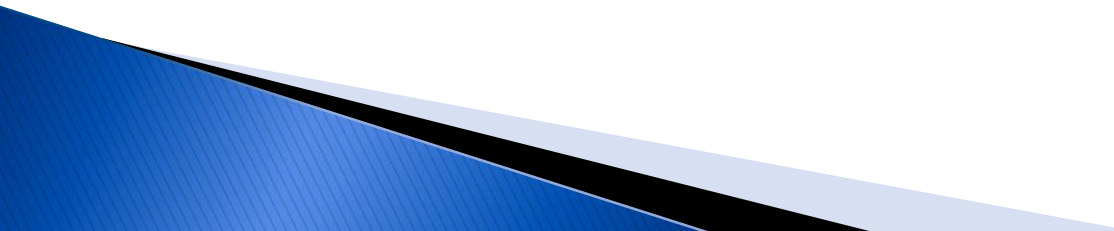
SBA 7(a) Advantages

- ▶ Relative simplicity and speed of approval. A seasoned SBA Lender can usually close a 7(a) transaction in 45 to 90 days (due to 3rd party reports).
 - ▶ A ready market for the sale of the guaranteed portion of the loan.
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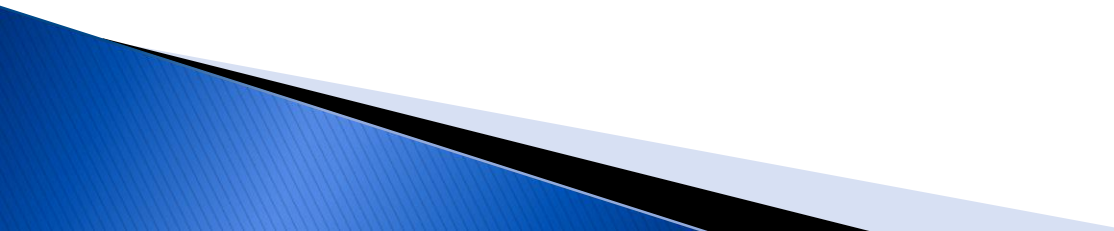
SBA 7(a) Advantages (Cont.)

- ▶ Higher net interest margins
 - ▶ Higher fee income
 - ▶ Reduced credit risk with either a 75% government guaranty (SBA 7a loan), or quick access to liquidity from the sale of guaranteed portions.
 - ▶ Reduced capital requirements
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How do I Become a SBA 7a Lender?

- 1) Contact your District Office
 - 2) SBA Form 750 and 750(b)
 - 3) Credit review based on your regulators
 - 4) Register for E Tran and CAIVRS
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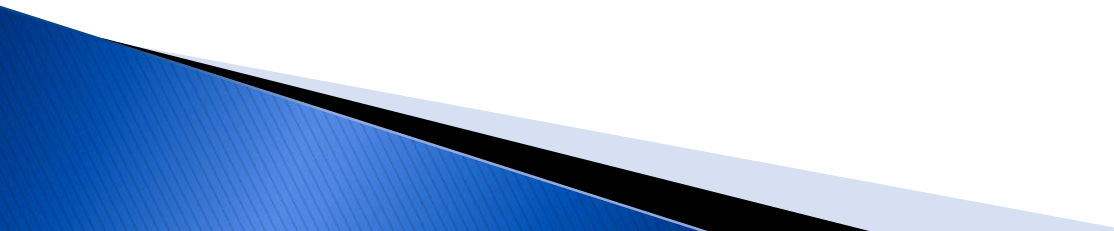
What are my Resources?

- ▶ District Office (they are all here!)
 - ▶ The SOP
 - ▶ The SBA.gov website
 - ▶ Webinars
 - ▶ NAGGL and regional trade organizations
 - ▶ Lender Service Providers
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What do I need as an Institution?

- Vision: What are my goals in participating in the SBA program?
 - Reaching underserved markets?
 - Doing more loans?
 - Increase profitability?
- Dedication of Personnel
 - The “go to” guy or gal (my opinion!)

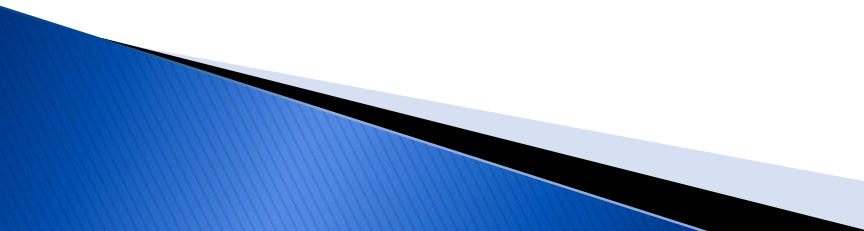
The Process

- ▶ Business owner approaches lender requesting a loan.
 - ▶ Lender (BDO?) reviews request, sees that it has merit.
 - ▶ BDO contacts Credit internally to discuss viability of the request.
 - ▶ For any number of reasons (discussed in a second), Credit determines that the loan could not be processed through the Lender's conventional loan credit channels.
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The Process Continued

- ▶ Credit and BDO (and dedicated person?) discuss what factors make this NOT a conventional loan and if SBA 7a can be used to make it a viable prospect.
- ▶ If credit concerns can be overcome with the addition of the 7a guarantee, the loan is underwritten according to bank standards, also allowing for SBA specific criteria (another few seconds please!)
- ▶ The Lender and Applicant complete the appropriate SBA forms for submission. At this time, Lender **MUST** get the 1919 completed for potential issues.
 - 912
 - Previous government financing (losses)
- ▶ Dedicated person (?) reviews final application for completeness!!!!

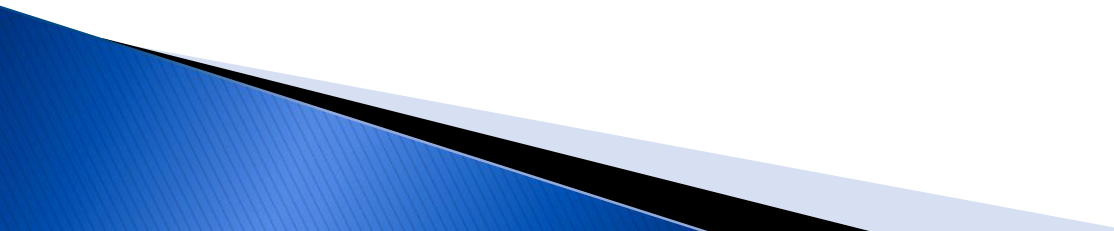
The Process Concluded

- ▶ Dedicated person submits the application to SBA via SBAOne (my preference) or E Tran.
 - Applications should be submitted using the 10-Tab Loan Application Submission format
 - Application documents must be uploaded into E Tran (if each document is less than 10MB) or sent via SBA's Send This File webpage (<https://www.sba.gov/content/send-file>)
 - ▶ SBA will typically turn around questions within 5 working days (my experience)
 - ▶ SBA issues the Authorization which outlines the terms and conditions with which the loan **MUST** be closed (review against Credit Memo carefully and request any changes in a 327 action).
 - ▶ Close loan preferably with an experienced SBA 7a attorney.
 - ▶ Prepare a 10-Tab!!
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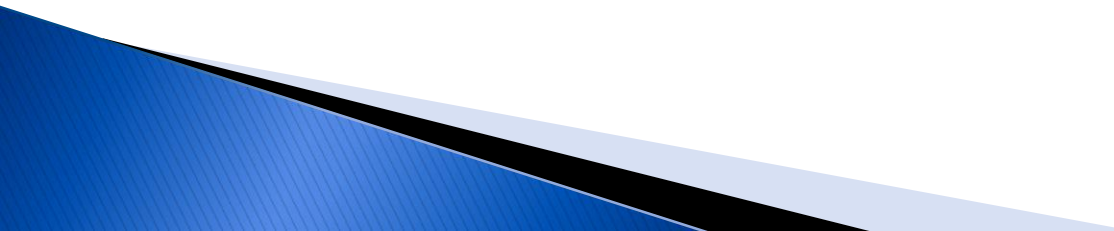
Reasons why SBA?

To even qualify for the SBA guarantee, the applicant cannot qualify for conventional financing from your institution.
Period!

Typical reasons for most institutions:

- 1) Needs longer term than is typically available for that type of loan.
 - 2) Insufficient collateral for conventional credit.
 - 3) Insufficient equity position.
 - 4) Industry specific exclusions.
 - 5) Previous credit issues.
 - 6) Loan Limits (not a stand-alone reason).
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The SBA Credit Memo

- ▶ Chapter 4 from K!
 - ▶ Pages 178–181 especially.
 - ▶ It's all about cash flow and significant “skin in the game”.
 - ▶ Must address credit elsewhere.
 - ▶ Must address adequacy of equity.
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Nuances of SBA Lending

- ▶ Collateral
- ▶ Guarantee fee initially
- ▶ On-going
- ▶ \$350,000 (credit scoring)
- ▶ Ineligible businesses
- ▶ Farming???
- ▶ Guarantees
- ▶ Cash flow minimums
- ▶ Franchises
- ▶ Construction
- ▶ 912
- ▶ CAIVRS
- ▶ Equity
- ▶ Environmental
- ▶ 159
- ▶ EPC/OC

Guaranty Fees 7a

1. Guaranty fee – Bank pays fee then is reimbursed by borrower. May be passed on to Borrower after first disbursement. Lender must use www.pay.gov to remit this fee.

–Term of 12 months or less - 1/4 of 1% (0.25%) of guaranteed portion – fee is due within 10 days of receipt of loan number.

–Term over 12 months (due within 90 days):

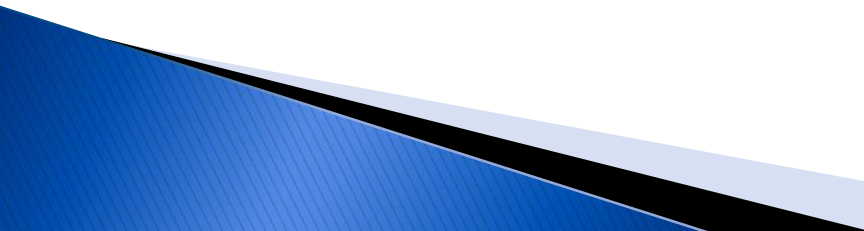
- Loans up to \$150,000 – 2% of guaranteed portion (Lender may retain no more than 25% of the fee)

- Loans between \$150,001 and \$700,000 - 3% of guaranteed portion

- For loans of \$700,001 to \$5 Million: 3.5% of the guaranteed portion up to \$1 Million, PLUS, 3.75% of the guaranteed portion over \$1 million

2. Ongoing fee of 0.55% (55 basis points) per year on the guaranteed portion of the outstanding balance; collected monthly – Paid by Lender – **may not be passed on to Borrower.**

Example: Rent Replacement

- ▶ Borrower is local attorney which rents a present location at \$3500/month.
 - ▶ Lender approaches Attorney and suggests that he buy his current location or build another once his lease expires.
 - ▶ Assuming the attorney has all his cash tied up in WC.
 - ▶ SBA would only require the business assets if loan is under \$350,000, but MUST conform to bank policy.
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Example: Rent Replacement

▶ Specifically:

- Existing Rent: \$3,500
- Purchase Building \$330,000
- Loan Amount: \$350,000
- Rate: P+1.75% 5.25%
- Term: 25 Years
- Monthly Payment: \$2,100
- Savings: \$1,400
- Potential Loan: \$575,000
- (with \$3,500/mo. Pmt)

The “Why” of SBA Lending

▶ Cash Flow

- Refi of Existing Debt
 - RE – 25 years
 - 10 years vs. 25 years = 42% improvement
 - M&E – 10 years
 - 3 years vs. 10 years = 64% improvement

**MUST not exceed useful life of assets being financed.

Example: Cash Flow

- ▶ The Lender approaches a potential customer which has a good deal of manufacturing equipment, all financed locally with another Financial Institution at typical 5 year amortization, but cash flow is tight, keeping this business from expanding.
- ▶ This loan amount is \$1,000,000, making his monthly payment \$19,332.
- ▶ Lender offers potential Borrower 10 year terms on same equipment.
- ▶ Finance \$50,000 for SBA fee, appraisals and legal to be conservative.

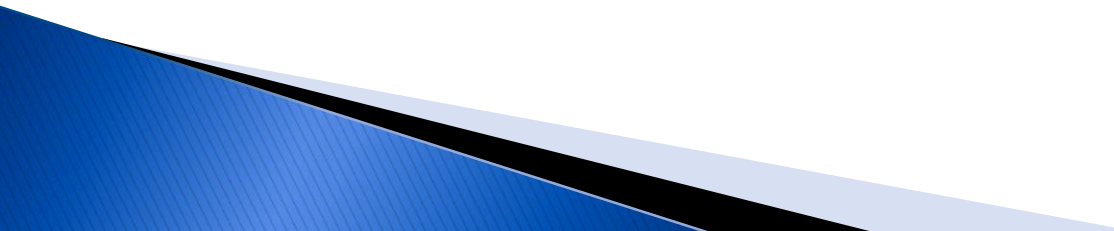
Example: Cash Flow

▶ Specifically:

- Existing Payment: \$19,332
- Refinance Loan \$1,050,000
- Rate: P+2.00% 7.50%
- Term: 10 Years
- Monthly Payment: \$11,657
- Savings: \$7,675

Flexibility

▶ Terms

- Fixed Rate Product/Blended Rate
 - Fixed for a Period of Time
 - Caps and Floors
 - Maturities (DSC)
 - Pay Fees
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Contact Us with Any Questions?

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