What is an SBA loan?

Most small business owners consider a variety of funding and credit options at one time or another. If you run a small business, you may have already heard about or considered Small Business Administration loans, also known as SBA loans.

For many reasons, SBA loans are a great choice for some businesses. To help you decide if they're the right choice for you, we've collected the benefits, drawbacks, application information, and other things you may need to think about when considering an SBA loan.

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Small Business Administration loan programs are drafted in agreement between lenders and SBA agencies. Borrowers use these programs when looking for lenders for their small businesses. Lenders appreciate SBA loan programs because the SBA shoulders some of the risk for the lender by guaranteeing a portion of the loan amount. Because of that guarantee, lenders are able to offer more flexible payment terms and lower interest rates than most small businesses would otherwise be able to get.

SBA loans and SBA Express loans are a useful option for many SMBs, but they do have several drawbacks that you should consider before applying. Here are some to think about before you make a decision.

PROS of SBA loans

- **Designed Especially for Small Business**
  SBA loan and SBA Express loans target small businesses. The SBA, in partnership with lenders, created guidelines with the aim of aiding small business expansion and growth. Unlike traditional bank loans, SBA loans are aimed specifically at SMBs.
- **Multiple Uses for the Funds**
  SBA loans and SBA express loans can be used for a wide range of expenses. According to the SBA, you can use these loans for "most" business purposes, including start-up, expansion, equipment purchases, working capital, inventory or real-estate purchases.
- **Secured Loans**

SBA loans are secured, meaning, SBA agencies guarantee a percentage of the loan amount to the lender, reducing their risk. (In cases where you don't pay what you owe, the bank can still seize your assets.)

- **Happier Lenders**
  Because the federal government guarantees SBA loans, more lenders are willing to offer financing to small businesses through SBA loans. In fact, lenders lower their qualification criteria for small businesses that apply for SBA loans.

CONS of SBA loans

- **Personal Credit Scores Required**
  In order to qualify for SBA loan and SBA Express loan, you must have a high personal credit score as well as good business credit. If either score is low, you may not be eligible.
- **2+ Years in Business**
  Your business must be at least 2 years old to qualify for an SBA loan. That can be a problem if you are one of the over 400,000 new businesses that appear every year in the United States and need operational capital just to get started.
- **Some Restrictions on Expenses**
  Some SBA loan programs have restrictions regarding the capital, meaning the money they provide can be used for specific purposes only. If your desired use doesn't fall within SBA restrictions, this isn't the right type of funding for you. The way you plan to use the funds may have an impact on your loan terms, so you'll want to think about this before applying for the loan.
- **Specific Eligibility Requirements**
  Even though it's generally easier to get approved for SBA loans than for traditional bank loans, the eligibility criteria can still prove to be tough for many small businesses to satisfy. The SBA determines eligibility based on criteria such as the nature of the business, where the business operates, and the character of the ownership. You can find more details about eligibility requirements for SBA loans here the official government website.
- Government Funding Coronavirus Relief for small business owners. Disaster SBA Loan.

By now, you're getting pretty familiar with SBA loans.

Next, you need to decide if these are the right choice for you. If you're an entrepreneur looking for the best way to fund your growing business, you might be wondering if an SBA loan will help you get where you want to be.

Do SBA loans work? Have they helped others? For many businesses, the answer is yes.

We went right the source for more information and exchanged emails with with the SBA Office of Communications and Bill Manger, associate administrator for the SBA's Office of Capital Access. Manger relayed a few impressive true SBA loan success stories:

- **Chobani Yogurt**, which had a valuation as high as $5 billion in 2016, used a 504 loan to start the company, according to Manger.
- **Vidalia Denim Mills**, a denim manufacturing company located in northern Louisiana, recently got a $25 million loan from the United States Department of Agriculture (USDA) and a $5 million loan from the SBA to grow their operations. The company "will be exporting its denim and employing more than 300 full-time workers thanks to its product and the partnership between the USDA and SBA," Manger says.
- **Laundry City**, a laundry pickup and delivery service based in Baltimore, benefited from a $3.5 million SBA 504 loan. The loan allowed to company "to grow and increase the number of its employees," Manger explains.

What are the different types of SBA loans?

There are several different kinds of SBA loans, so choosing the one that works best for your business can be a bit tricky. How do you find the right loan for your specific situation? You'll want to understand the options before you decide what's right for you.

"Small businesses seeking financing should speak with their lender about their individual needs," Manger advises. "The SBA provides guarantees on loans that lenders would not make on a conventional basis."

To help make your decision easier, we've put together a list of eight of the more common forms of SBA loans at the time of this writing. That said, the SBA does change its offerings from time to time as the market dictates, so always check with them to be sure.

“The SBA modernizes its loan program periodically to reflect the current market,” Manger says.

When offerings change, the SBA provides updated information to lenders, who then provide it to the applicants, according to Manger.

“Applicants can reach out directly to one of our 68 field offices or find information available on the SBA.gov website, which has the standard operating procedures for our loan programs,” Manger explains.

To expedite your loan application, start with a look at the list of SBA-approved lenders here. For the fastest results, be sure to have all of the necessary documentation on hand before you apply.

1. SBA 7(a) Loans

The most common loan available through the SBA is a 7(a) loan which provides $30,000 to $5 million to small business owners. Qualified companies can use the funds to fund startup costs, purchase equipment, buy new land, repair existing assets, expand an existing business, acquire a new business, refinance debt, purchase inventory and supplies, and more.

To qualify for financing, business owners need to have good credit and good business history. In most cases, borrowers will have to put up collateral in order to secure financing.

Generally speaking, repayment terms do not exceed 10 years for most loans and 25 years for real estate loans. Interest rates can fall anywhere between 5–10 percent.

2. SBA 504 Loans

Small businesses that need long-term loans for fixed asset acquisitions—like buying property, buildings, or heavy equipment—can find the funding they need through the SBA 504 Loan program.

If approved, they can qualify for up to $5 million in financing. In most instances, owners are required to guarantee at least 20 percent of the loan.

“These loans are made available through Certified Development Companies (CDCs), which are the SBA’s community-based partners,” Manger explains.

"The advantage of this program is that it provides terms of 10 years, 20 years, and 25 years, which helps free up cash flow for small businesses."

To qualify for funding, businesses can not be worth more than $15 million and they must have an average net income of $5 million or less after taxes over the two previous years, according to the SBA. Nonprofits and businesses engaged in passive or speculative activities can't get 504 loans.

SBA 504 Loans have fixed rates attached to them. You can use them in a variety of ways, including:

- Purchasing buildings
- Purchasing land and land improvements, which include grading, street improvements, utilities, parking lots, and landscaping
- Building new facilities or renovating existing ones
- Buying machinery or equipment that you intend to use over the long term
- Refinancing debt that stems from expanding a business through facilities or equipment

The 504 program, however, comes with some restrictions. You can not use these funds to buy inventory, consolidate debt, or as working capital.

According to the SBA, businesses usually need to create or retain one job for every $65,000 in financing they receive via 504 Loans; small manufacturers need to create or retain a job for every $100,000 in SBA funding.

In lieu of that, CDCs fund businesses that meet community development goals—like improving or stabilizing the economy, stimulating the development of other businesses, or bringing new income into the community. CDCs also fund businesses that help them meet their public policy goals, including revitalizing a community, expanding exports, increasing businesses owned by women, veterans, or minorities, and aiding rural development, among other things. What's more, CDCs are more likely to approve loans that help them update facilities to meet health, safety, and environmental requirements.