

## **Chapter 4**

# **SMALL BUSINESS ADMINISTRATION**

## **INTRODUCTION**

In this chapter we will discuss how Small Business Administration (SBA) loan programs provide capital by reducing the risk of commercial lenders. Eligibility for SBA loan programs and prohibited loan uses will be discussed as will the mechanics of applying for an SBA loan. We will discuss SBA's criteria for granting loan guarantees and how they apply to a variety of loan programs.

## **OVERVIEW**

The Small Business Administration (SBA) does not lend money.<sup>1</sup> It provides a guarantee on money lent by commercial institutions. Since lenders constantly weigh risk and reward, anything that reduces risk improves the likelihood that a loan will be granted. On the other hand, a business must clearly demonstrate their ability to repay a loan. Even where the SBA guarantees 80% of a loan, the lender will not want to lose the remaining 20%, nor will it want to service loans with collection problems.

So how does an SBA loan guarantee help? Some loans are clearly worth granting with or without an SBA guarantee and some would be declined under any circumstances. SBA guarantees are useful for those companies that are almost, but not quite good enough to qualify for a

conventional loan. For those, an SBA guarantee can tip the balance in favor of granting the loan.

SBA guarantees also make it possible for banks to extend repayment terms. Where a bank may only grant a conventional loan for four or five years, it might extend terms for an SBA guaranteed loan to six or seven years. The length of the loan will be a function of the loan purpose and the assets it finances.

**ELIGIBILITY**

Before a company can use an SBA loan program it must meet two types of eligibility criteria. First, a business must qualify as a small business within the meaning of the Small Business Administration Act and the regulations promulgated there under. The second criterion is that SBA loan programs can't be used in certain industries or for prohibited purposes.

**What Constitutes a Small Business?**

There are limits on the size of companies that qualify for small business loans. Limits vary by industry, and limits are stated in terms of both number of employees and revenue. Figure 4-1, Small Business Size Limits, provides some examples of maximum size limits by industry.

Figure 4-1 Small Business Size Limits

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|                             |                            |
|-----------------------------|----------------------------|
| Manufacturing and Mining:   | 500 employees              |
| Wholesaling:                | 100 employees              |
| Services:                   | \$6 million in revenue     |
| Retailing:                  | \$6 million in revenue.    |
| General Construction:       | \$28.5 million in revenue. |
| Special Trade Construction: | \$12 million in revenue.   |
| Agriculture:                | \$0.75 million revenue     |

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