SBA 7A / SBA 504 & Traditional Financing
Comparison of Options

Here at CLX we often get asked the differences between SBA 7A, SBA 504, and traditional bank financing. There are many positives and negatives of each program. We have put together the following information to provide some basic parameters of the programs, as well as outline what we see are the positives and negatives of each option to help you decide what will work best for you.

SBA 7A Loan:

- The SBA 7A loan program is used to help start-up and existing small businesses purchase new land & build a building, purchase a building, repair existing capital assets, purchase or expand an existing business, refinance existing debt, provide working capital and purchase machinery, furniture, fixtures, supplies or materials.
- A bank will make the loan with this program, while the SBA guarantees 75% of the loan amount, providing the bank a guaranty that a large portion of the principal will be repaid if the loan goes into default.
- Businesses must meet size standards and be considered small within their particular industry.
- Must operate for profit, be engaged in doing business in the United States, have reasonable equity to invest, and must have tried to use other financial resources, including personal assets, before applying for a loan.
- Requires personal guarantees of the owners with 20% or more ownership interest in the business.
- For real estate loans the property must be 51% or more owner-occupied.

Benefits	Negatives
Requirement to only put 10% down of the total project cost.	Roughly 3.5% guaranty fee on the SBA guaranteed 75% of the loan amount (this is an SBA fee that they use to cover losses on the program). This fee gets rolled into the loan.
25-year loan term that really cannot be called sooner unless you default on the loan, change ownership, or one of the guarantors dies (or a few other reasons). So there are no on-going conditions to meet so long as you stay current.	Most likely a variable interest rate during the loan term that is higher than bank rates to start, but on occasion a fixed rate can be gotten.
Flexibility to roll other costs into the financing including moving expenses, working capital, equipment, debt refinance, etc.	Borrowers are limited to $5 million in SBA exposure. The full loan amount counts against a Borrower's SBA loan exposure so the maximum project a Borrower can support with only 10% down on an SBA 504 loan program is $5.55 million.
More flexibility in getting approvals done because the bank requirements are less on an SBA 7A loan due to the government guarantying 75% of the loan versus the SBA 504 program where the bank still has exposure on 50% of the project cost.	For real estate loans, pre-payment penalty in the first 3 years of 5% year 1, 3% year 2, 1% year 3. No penalty after year 3.
No limit on the loan to value you can fund with the program.	
Limited prepayment penalty that only exists during the first 3-years of the loan.	
One loan to repay instead of two under the SBA 504 loan program.	

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SBA 504 Loan:

- The SBA 504 loan program is an economic development loan program that offers small businesses another avenue for business financing, while promoting business growth and job creation. SBA 504 loans are used for purchasing real estate, renovations / improvements to existing real estate, and equipment financing.
- This program is made available through Certified Development Companies (CDCs), who work with the SBA and participating lenders to provide financing to small businesses.
- A bank will lend 50% of the total project cost and be in 1st position on the mortgage; the CDC will lend 40% of the total project cost and be in 2nd position on the mortgage. The bank will fully fund both portions of the loan at the time of closing until the CDC raises the funds through a bond sale to fund its portion, which can take anywhere from 30 days to 6 months after closing.
- Must meet size standards and operate for profit.
- Requires personal guarantees of the owners with 20% or more ownership interest in the business.
- For real estate loans the property must be 51% or more owner-occupied.

Benefits	Negatives
Can finance 90% of the total cost to acquire and improve the property. Sometimes can finance in some limited equipment as well.	SBA guaranty fee of roughly 3.5% of the SBA 504 portion of the loan (this is an SBA fee that they use to cover losses on the program).
SBA portion of the loan (up to 40% of total cost on a purchase and/or construction) on a 20 or 25-year fixed rate at typically a rate below market.	10-year pre-payment penalty on the SBA 504 portion of the loan, with 100% of the yield rate in year 1, 90% in year 2, and so on. After year 10 there is no longer a pre-payment penalty.
Bank must commit to give you at least a 10 year loan term on their 50% of the total project cost (versus typically a 5-year loan term on a traditional bank loan) with the rate fixed for 5 years.	You end up with two loans versus one loan conventionally or with the SBA 7a loan program.
There are no covenants or on-going conditions that have to be met on an SBA 504 loan other than staying current on payments, no change in ownership, continue to owner-occupy more than 50% of the building, and no death of the guarantor(s) (along with some other minor default conditions).	The interest rate on the SBA 504 portion of the loan is not fixed until 30 to 45 days after acquisition or after all improvements are completed. Debenture sales happen the first Tuesday of every month and the rate is set at the next closest Tuesday after acquisition or improvements are completed within that 30 to 45 day window typically.
Easier to get approvals done versus conventional bank financing because the bank is only at a 50% loan to cost on the project, so the loan is deemed lower risk.	The bank loan may have a pre-payment penalty as well (versus the SBA 7A loan where the penalty is only 3 years).
Borrowers only have $5 million in available SBA debt. Since only 40% of the cost is funded by the SBA, the total project cost can be as high as $12.5 million with only 10% down versus the SBA 7A option where the maximum cost with only 10% down is only $5.55 million.	The bank loan will mature after 10 years, requiring a refinance of that portion of the debt. The loan may also re-price after the first 5 years. The bank may not renew the loan at the end of 10 years so that loan may have to be refinanced (as opposed to the SBA 7A loan that is a 25 year term).
If a borrower decides to refinance the bank first mortgage, the SBA will typically re-subordinate their second mortgage to a new lender so long as there is no cash out with the refinance.	The bank could have covenants or conditions a borrower has to meet on their portion of an SBA 504 loan and if those conditions are not met (including certain cash flow conditions) the loan could be called by the bank.
Can go up to 100% of the "As-Completed" value on the appraisal.	Must get the loan approved by both the CDC as well as the bank.

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Traditional Bank Loan (Owner-Occupied):

- Financing provided by traditional banks and lenders. The most common form of financing for small to mid-sized businesses.
- Requires strong personal and/or business credit scores, personal guarantees, collateral and healthy financials.
- Requires personal guarantees of the owners with 20% or more ownership interest in the business.

Benefits	Negatives
Only one credit decision to be made by the bank. They do not need any additional loan approvals from the SBA.	Typically 20% to 25% required down payment of total cost.
No government guaranty fees to be paid as part of the loan (as opposed to roughly 3.5% of the loan amount for the SBA 7A and SBA 504 options).	Loan typically cannot exceed 75% to 80% of the "As-Is" (or the "As-Completed" in cases of construction) appraised value of the property.
Typically slightly quicker to closing due to the fact that the SBA is not involved.	Slightly harder to get loan approvals done because the bank is taking on the risk for the entire loan amount.
No long-term pre-payment penalties so the borrower is not locked into a loan program long-term.	Loan term typically not longer than 5, 7 or 10 years. Amortizations typically 20 to 25 years.
Flexibility on structure and typically attractive fixed rate options available.	Bank can include conditions or covenants in the loan the borrower must meet post closing.