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Navigating opportunities within recent SBA loan changes

What small business owners need to know about recent shifts and how to make the most of the new possibilities they present

Last year, the U.S. Small Business Administration (SBA) provided nearly $43 billion in funding to the country's small business owners. In its 70-year history, the agency has helped countless entrepreneurs support their business vision by providing access to government-backed loans from lenders. However, the SBA's arduous application process and restrictive rules can often end up excluding worthy borrowers. Enter the program's recent changes, which took effect Aug. 1, that are poised to transform the way in which lower down payment and longer repayment loans are approved.

Though the SBA loan program has, to date, already helped millions of people realize their small business goals, these changes are expected to vastly increase access to capital for a new swath of entrepreneurs. In essence, the SBA loan program has been both streamlined and expanded, removing certain bureaucratic burdens from lenders' shoulders, boosting the community focus of the loan program and expanding borrower criteria to put loans within reach of more business owners than ever before.

But while the SBA changes will almost certainly have a big impact on borrowers, many small business owners may not yet be aware of their implications and the new opportunities that these changes present. To shed more light on these landmark shifts in SBA lending, this paper will explore four high-potential areas that are well worth a second look for entrepreneurs.

1. It's easier than ever to qualify for a loan — and these changes help to level the playing field

Then: Generally speaking, the previous SBA loan borrower criteria was more restrictive than the criteria now in place, a situation that often served to exclude borrowers from receiving the SBA assistance they needed. Further, it was clear that eligibility requirements needed to shift because of the disparities in who received SBA loans — and, more importantly, who didn't. For years, men received 70% of all SBA 7(a) and 504 loans, and small-business owners of color consistently received loans less frequently than borrowers as a whole.

Now: Lenders will now consider fewer factors when qualifying borrowers for 7(a) and 504 loans, narrowing the list of nine factors to determine creditworthiness down to just three: credit score or credit history; earnings or cash flow of business; and collateral. Previously, other criteria included current invested equity, past financial statements and subjective factors like the business owner's level of experience.

Not only do experts predict that these shifts will widen the range of borrowers to include more women and people of color, but the changes also have the potential to dramatically bolster the small business landscape, with far-ranging effects on the American economy — especially considering that small companies are responsible for creating 64% of new jobs.

Why the push to make lending more accessible? Thomas Huffman, executive vice president of Wintrust's lending division, attributes the shift to a desire to help small businesses thrive. "To my understanding, the changes are designed to get some of these government loans to people who need them most," he says. "What percentage of SBA loans are made to Black Americans? What percentage are made to women-owned businesses? And is the rate at which they receive loans proportional to how many small businesses they own? Not necessarily. That's the kind of disparity the SBA is trying to rectify."

2. Management or partner buyouts are now far simpler

Then: Obtaining an SBA 7(a) loan to buy out a partner was once a highly complex and often painstaking process. The partner planning to exit the business would need to first leave the company fully, then be paid for their share — a counterintuitive rule that often made for a slow severing with the potential to destabilize the business. Meanwhile, even securing a loan was often tough, since the departure of a business partner can have the unintended effect of putting lenders on alert: Is the partner leaving because the business is struggling? Could the partner's departure damage the business's standing?

In addition, old SBA rules stated that to qualify for a loan to buy out a partner, the business must possess at least 10% equity. This could make landing an SBA loan extremely difficult without the remaining partner putting up their own personal funds to satisfy the requirement, which not everyone can readily do.

Now: With the changes enacted this year, partners no longer need to leave the business to be bought out of the company. In other words, securing a buyout loan doesn't require a "complete" change of ownership, but merely a partial change of ownership. What does this mean for business owners? Those with often the greatest amount of institutional wisdom are now allowed to stick around to create a more orderly transition, and no one is being asked to come up with a prohibitive amount of cash to proceed with a sale.

"This new provision helps partners plan ahead while they're anticipating selling their business," Wintrust Vice President of SBA Lending Beata Gesicki says. "They can determine if they want to continue to have some kind of ownership in the company. Will they do it at 100%? Or will they only do it partially, and still keep some portion of it?"

This shift also has positive implications for succession plans nationwide, Huffman says. "About half of all American small businesses are owned by people over the age of 50," he says. "And if we as a society don't figure out how to transition some of those businesses, a lot of them are just going to close. That's going to be a drag on our economy because a lot of jobs will be lost." Making it easier for, say, a founder's child to buy out his or her parent or a manager to purchase their aging boss' business is a shrewd way to avoid that potential scenario.

The most common types of SBA loans, explained

SBA loans come in a variety of shapes and sizes, including differences in borrowing limit, approval process time and allowable uses. Here are the features of some of the most popular SBA loans.

7(a) Loan

The SBA's most popular loan, this product provides capital to businesses in need of a maximum of $5 million in assistance (though most borrow less). These funds can be put toward everything from real estate purchases to new machinery or supplies, refinancing existing debt, or injecting a cash infusion into the business during a difficult period.

SBA Express Loan

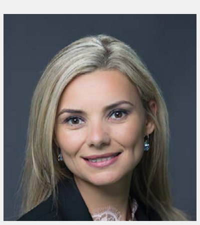
This loan, capped at a $500,000 borrowing limit, comes with an expedited approval process, which is a boon for times when businesses need capital urgently.

504 Loan

Ideal for bigger investments such as real estate or large equipment (known as "fixed assets"), this loan is intended for major investments in the borrower's business.

Microloan

Small loans — the average size is $13,000 — that can be used for typical needs such as purchasing supplies or bolstering inventory, but not for paying off debt or purchasing real estate.



"This new provision — requiring only a partial change of ownership to secure a buyout loan — helps partners plan ahead while they're anticipating selling their business. They can determine if they want to continue to have some kind of ownership in the company."

-Beata Gesicki, Wintrust Vice President of SBA Lending

3. Refinancing is more easily within reach

Then: Historically, real estate debt incurred via an SBA 7(a) loan could only be refinanced with an SBA 504 loan, and organizations who wished to refinance through the SBA had to meet a bevy of requirements, such as having accrued debt that was at least two years old.

Now: In light of the recent SBA changes, borrowers can now refinance an SBA loan to pursue more favorable terms without many of these strict requirements. For example, the business's debt only needs to be six months old, instead of two years; the entirety of the debt can now be refinanced, instead of only 50% of it; businesses no longer need to be current on all payments in order to be approved for refinancing; and other SBA loan products, such as 7(a) loans, can now be refinanced with another 7(a) loan.

However, Huffman indicates that this scenario will likely apply mostly to businesses that are doing well already and are looking to refinance their loans as a means of growing their reach.

"Say I own three coffee shops and I want to open a fourth, but my current bank won't give me the money," Huffman says. "I go to a new bank, and the bank says, 'Well, I'd really like to give you the money for the fourth, but I'd rather have all your business. So, I'd like to pay off your existing SBA loan, give you some new money, and then you'd have one new loan secured by all four of your coffee shops.'" In other words, while the refinancing rules have certainly loosened, the process will likely be of greatest benefit to companies that are already firmly established.

Three SBA loan borrowers weigh in on their Wintrust experience

Loan Type: Buyout

Emilie Roche
Road Fabrics, Inc.

"I met the owner and founder of Road Fabrics five or six years ago, and he explained how unique the company was. When I heard in 2022 that he wanted to sell his company, I offered to buy it. I wanted to preserve his legacy and build my own. To make that happen, I took out a 7(a) loan with Wintrust, which was the best option for us. It benefits the borrower because having interest rate caps helps keep costs affordable for our side, and there are guarantees for the lender, too, which reduces their risk and helps get the loan approved. Plus, Wintrust is a preferred lender through the SBA program, and they really made the process seamless. I could reach out to them with a question, and they'd shoot back a response within the same day."

Loan Type: Real Estate Purchase

Jon Bohlen
A.D. Kenwood
(dba Valvoline Instant Oil Change)

"We're a retail automotive maintenance provider, and to do our business, we need retail locations. Sometimes we build them from the ground up, and sometimes we find an existing oil change business, buy it, then convert it to our brand and our system. Either way, it takes a certain amount of capital, and like most businesspeople, the amount of capital I can deploy is limited. So, I borrow money. Otherwise, our growth would be much slower if we had to wait until we accumulated enough capital to do it without financing. I went with Wintrust because it's the largest SBA lender in the area. I've had a few SBA loans, but I really don't know much about the SBA. I answer the questions that are asked, I provide the documents they request. I then borrow the money and I don't think any more about it. But that's kind of the point: Because of Wintrust, I don't really have to know much more than that. They make it seamless."

Loan Type: Business/Strategic

"There were several factors that all came together at once. We had acquired a business in Michigan in 2021 that you might say was a turnaround. We moved them to Illinois. We bought a building. We experienced significant growth. With that growth, we had to acquire more equipment. And with the inflation at the time and us trying to turn around this company, our margins had shrunk. We had a need for a change in our capital financing arrangement, and it just didn't fit the model of traditional financing very well. So, the president of our local branch of Wintrust presented us with the SBA program. We moved forward with a loan, and the experience was excellent. Wintrust has a lot of experience, and they did all the legwork. I provided them with what they needed, and it was smooth and painless for me."

Mike Abrahams
Excelsior, Inc.

> "About half of all American small businesses are owned by people over the age of 50, and if we as a society don't figure out how to transition some of those businesses, a lot of them are just going to close."
>
> **- Thomas Huffman, Wintrust Executive Vice President of SBA Lending**

4. Strategic acquisitions are now far less onerous

Then: Prior to these changes, using an SBA 7(a) loan to acquire a separate business entity was difficult for a number of reasons. These kinds of loans required long approval processes, as well as a vast volume of financial documentation. The SBA also had highly complex requirements for the financing structure of the loan, including the need for the borrower to acquire 100% of the acquired business and bring at least 10% of its value in capital to the transaction's closing, a requirement known as the "equity injection."

Now: To encourage more widespread business expansion and overall economic growth, the SBA now explicitly states that no equity injection or seller financing is required when acquiring a company with the same North American Industry Classification System (NAICS) code as the buyer's existing business in the same region. Many lenders had this rule in effect already, but this more formal adoption will inspire many other lenders to put it in place.

While the new changes to the SBA loan program are significant — and will almost certainly make obtaining financing for one's small business easier — the process of applying, being approved for, and allocating these funds appropriately can still be daunting for anyone new to the experience. And, of course, with government-backed loans comes a vast array of paperwork, due diligence, patience and various personal requirements to meet (often including taking out a life insurance policy, for example, or contributing private funds).

That's why it's essential that small business owners align themselves with a known SBA expert like those at Wintrust, who can translate this process into a streamlined, simple undertaking. Luckily, given these groundbreaking recent changes to the SBA program, it's ever more likely that borrowers will qualify for the capital they truly need to grow their businesses — and that spells good news for small businesses across the country, as well as the economy as a whole.

Wintrust has the know-how to guide you through the loan process and secure the precise solution your business needs to thrive.

SPEAK WITH A LENDING EXPERT TODAY

Simplified, Better Accessibility:
How businesses can benefit from new SBA loan changes

Are you an entrepreneur considering a SBA loan to help grow your business?
Have you heard about the recent modifications to the program, but are unsure how they might affect you?

Join Wintrust and Crain's Content Studio for a webcast that will help explain these major shifts that both simplify and expand the popular federal loan program. Wintrust's SBA loan executives and customers will share their expertise and experiences navigating the process.

Registration is free but required in advance.

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