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Brendan Brandt, Managing Partner
Peter Shahram, Esq., Senior Associate
Bryan Shea, Senior Associate

Small Business Administration Introduces Reduced Equity Injection Requirements for Business Acquisition Loans

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The recent changes to the Small Business Administration (SBA) 7(b) lending program have improved access to funding for individuals and businesses in search of a low cost, low down-payment source of business acquisition capital.

Beginning January 1, 2018, the SBA has enacted a new and revised Standard Operating Procedure (SOP) 50 10 5(J). The key changes of the updated SOP include significantly lower equity injection requirements from buyers financing a business acquisition and a change in the "seller standby rule" which has been extended from two years to the entire life of the loan.

Under the updated lower equity injection requirement, buyers searching for financing to fund a business acquisition will find that the newly revised SOP only requires a minimum equity injection of 10%, thus allowing buyers to finance up to 90% of their acquisition from banks under the SBA 7(a) program. Additionally, at least 5% of the overall injection must be from the buyer's own resources, effectively brining the buyer's minimum required cash contribution to just 5%.

The previous SOP for a business acquisition required for buyers to put up a 25% equity injection for deals in excess of $500,000, and a 20% equity injection for deals under $500,000. Overall, the new SOP reduces the buyer's equity injection requirement by between 10% and 15% (15% and 20%).

The second major revision to the SOP requires that any financing provided by the seller that is to be included as part of the buyer's 10% equity injection, such as a seller note or a carryover note, will be on standby for the entire life of the SBA loan period.

Under the prior version of the SOP, the "seller standby rule" only required that seller carry notes be on full standby for at least 2 years behind the SBA loan, whereby collecting no payments of principle or interest. This substantial revision from a 2 year standby, to a the new standby period which lasts for the loan's duration, may discourage seller financing in business acquisitions under the 7(a) lending program.

To illustrate the significance of the newly revised SOP in financing acquisitions, let's assume an acquisition purchase price of $2,000,000. Under the previous SOP, the buyer was required to provide a 25% equity injection of $500,000. However, as of January 1, 2018, the buyer is only required to provide a 5% cash down payment of $100,000, in addition to a 5% seller note for $100,000. A savings of $300,000 over the old SOP.

These changes to the SBA 7(a) lending program are likely to have a significant and positive effect on buyers seeking business acquisition financing and the strategic approach M&A advisors take with their clients.

At Epsilon Acquisition Services we have cultivated strong connections with banks designated by the SBA as preferred lenders under the Preferred Lending Program (PLP). Utilizing the expertise of our advisory team at Epsilon A.S., we can guide you or your business through the complexities of the acquisition process from deal identification and financing arrangement to due diligence, deal structuring, and back end advisory services.

Contact us today for a free, confidential consultation.

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