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What To Do If You Can't Make Your SBA Loan Payments

by Gerri Detweiler on 05/30/2011

Across the country, many business owners are fighting not only to keep the doors to their businesses open, but to keep up with payments on their business debts. Falling behind on an SBA loan can be particularly scary because it may be one of the largest debts the business owes, and because these loans often involve personal guarantees and collateral.

Here's what you need to know if you've taken out an SBA loan and can't keep up with the payments.

Because SBA loans are guaranteed by the federal government, misconceptions about the collection process abound. "There are a lot of people who have this fantasy that the government is going to pay it so they can just try again next time, but that's wrong," warns Charles H. Green, director of the Small Business Finance Institute.

In most cases, if you fall behind, you'll be working with the bank where you obtained the loan, and not the SBA itself. "The SBA will not come knocking on your door," says Denise Beeson, a commercial loan officer at Baysierra Financial. Green agrees, adding that "The SBA used to do all liquidations, but that's moved to preferred lenders. SBA is pretty much just in the business of doing accounting and letting the bank work it out."

A personal guarantee is required on "the vast majority of SBA loans," says Lendio president Levi King. "The only rare exception would be businesses with tons of collateral, lots of time in business, and super clean financials." That means the lender may be able to look to the borrower's personal assets, as well as business assets, to try to collect.

In addition, many borrowers pledge either personal or business property as collateral. If you pledged collateral for the loan "they may actually seize your collateral," warns Beeson. Be-

fore the lender tries to do that, however, it may be willing to work something out. Green points out that the banks are often less interested in trying to repossess heavy or specialized equipment, which will then have to be disposed of in a timely fashion, than they are in trying to recover as much as possible of the defaulted loan.

Typically, the collection process begins as soon as you miss a payment, says Green. Once the loan becomes 60 – 120 days delinquent, collection efforts intensify. The lender may declare the loan in default and request the guarantee from the government, but it will still try to collect as much of the balance as possible.

You typically won't hear from an outside collection agency, says Greene. "Banks typically don't outsource collections on business debts. They usually have a special division that handles collecting the loan. (Unlike the loan officer) they are impartial, and don't have a personal relationship with the borrower."

King describes the collection process as "a lot like that for any other bad business debt that is personally guaranteed. First they'll foreclose on any collateral that was put up to secure the loan, then they'll sue the business for default, then they'll sue the guarantor(s) for default, and they'll get a judgment against the business, guarantor(s) or both."

If the bank is able to collect anything from the borrower, 75% will go to the government to repay the guarantee and the bank will keep the other 25%, explains King.

So what are your options if your business is floundering and you can't repay your SBA loan?

Workout or Settlement: You may be able to resolve your debt by paying less than the full amount you owe, either by negotiating directly with the bank yourself, or with the help of an attorney, your CPA or another advisor. "Go to the bank," says



Ken Thomson, founder of Biz911 and author of *The Battle Scarred Guide to Small Business Debt Relief and Recovery*. "Really get to know the people involved. Go the extra mile to give them the information that they need to have to make a favorable decision." He explained he had success with this approach last year, with a client who had an importing business and a 7(A) loan.

Green encourages business owners to "Raise your hand a little earlier and reach out for help. Don't wait until your back is against the wall. You have a lot better opportunity to work something out if you talk with your banker earlier," he says. He points out that "they've got a vested interest in the outcome. Business is business."

Keep in mind that you will likely receive a 1099-C for the forgiven debt, warns King. That may result in a new tax liability to the IRS.

File for Bankruptcy: "The personal liability for an SBA loan can be discharged," says Barry J. Roy, Esq, a bankruptcy attorney and partner with the law firm of Rabinowitz, Lubetkin & Tully LLC. The borrower may, for example file bankruptcy individually and the company would still be liable for the debt. "It may not always be an easy decision," he points out. "You may lose property that is not exempt." However, for someone facing a large debt that can't be repaid, it may be the only way to get a fresh start. You will not owe taxes on forgiven debt discharged in bankruptcy.

Once you default on an SBA loan, it's unlikely you'll be eligible for another one in the future, especially if the SBA suffered a loss.