Buyer requirements in today's markets

Previous and future changes that affect them

By Steve Mariani

If a potential buyer would have called our office just a few years back we would have advised them completely differently than we would today, so what's changed since then? Everyone reading this should know the biggest change over the last years has been a reduction in the SBA required down payment amount. This was actually reduced on "change of ownership" transactions from 25% down to 10% as of January 2018. The question then becomes, what amount will the lenders accept on a business acquisition transaction. What we've found over the past year and a half is that this varies greatly from lender to lender and deal to deal. When we're asked about down payment amounts from any potential buyer or broker our answer remains consistent, our default is 15% (but could be less) and today I'll explain why.

Let's start with the three most important items we explore with every borrower we work with. Some may take assistance to complete but in every deal with every lender, these items are always required.

1) Good credit. Maybe not absolutely perfect, but good enough to show a level of financial responsibility that can translate into a lender's assurance of repayment.

2) Experience that relates to the new business. The unwritten rule amongst lenders is that they would like to see at least one year of direct industry experience OR three years of related experience within the last five years

3) The down payment. If the buyer has the down payment money available, then this requirement gets checked off. But if he is considering investors or partners then the waters get a bit cloudy and need additional conversations.

At this point you should be wondering why we default to 15% down as opposed to quoting the lowest of 10%, which is required by SBA. Here's why and how we explain this to our clients. Can we provide financing with only 10% down, yes, and we do it often, but it is not where we begin. Many transactions do secure financing at 10% down but setting the expectation and understand all the remaining pieces of the transaction will many times require an adjustment of the down payment. If all three of the above items are in line and fit perfectly with the acquisition target, we're happy to present this deal at 10% down and will most likely secure an approval.

What if our buyer does not have direct experience or maybe the business had a concern last year that caused a downturn in revenues? Maybe the buyer has an excellent resume' but needs an outside source to secure down payment assistance?

These are just a few of the items we see as lender concerns that will need to be addressed as we move forward. Not being a direct lender allows us to consult more deeply with a potential buyer and explain what our goal is and how to correctly outline steps to bring this to a successful conclusion. Most lenders will not explain any rule that works against their internal policies and therefore we find they only explain the rules affecting that specific lender.

Working with many high net worth borrowers, there is another rule being reconsidered as we speak that will affect every transaction these borrowers consider. This rule was previously in affect until the SBA removed it to allow for the financial recovery of the business markets after the 2010 crisis. This rule is written as the "personal liquidity" test and previous versions included the following verbiage: If the loan amount exceeds $500,000 then the borrower must also inject any amount over the down payment that is above the total financing package amount or $750,000, whichever is greater. Should this rule be reinstated, it would make many of our current, eligible borrowers', ineligible for SBA assistance.

A buyer's resume can be very misleading. We will always require a phone conversation about a bio to better learn and understand each buyer's qualification level and skillset. We've found that most borrowers don't know exactly what to include on an updated resume' to convey the relatable experience level to their target business. With this concern in mind, we interview each buyer and advise them on what should and should not be included as this is one of the SBA's hotter topics this year. Although many times we can address the lack of direct industry experience, we will have to provide a comforting level of management skills and employee relations for most transactions to any potential lender being considered. A buyer's resume' is very important when it comes to securing an approval so at a minimum, be sure to educate your client.

Credit reports are often times blatantly wrong and we see these errors many times each year. Once we've determined the credit score of a buyer is below the minimum for that specific lender, we want to understand how we can correct it. Is there only one item of concern on the report or is this buyer always late on every account they have? Much of the country, at one time or another, has gone through hard times and many of these has affected a great buyer's credit score. Is there specific events that led up to the delinquent account of concern? Over the years and fluctuations in our economy, lenders have become much more understanding of specific circumstances that can affect a person's credit. Many times, an explanation is enough to bring a lender comfort and allow the request to continue being processed, sometimes not. The important thing to understand about credit is that it's something that needs to be addressed right up front. No one wants to learn about it 30 days after the loan request has been submitted, the sooner it is discovered, the better for all parties. A credit report is something we require within the first 24 hours of speaking with any potential client and can adjust each day after that based on the results.

The three items I've described today is the initial conversation we have with any potential buyer and we will cover all three during that call, always!

Why do we default to 15% down when asked? The easy answer is to make up for any shortfall or concern a lender may have in any of these three items and or business concern they might have during underwriting, it secures more consistent approvals.

We hope this newsletter helps you close more transactions and PLEASE donate to my MS ride this month, I only have a few weeks left and need your support.

Steve Mariani

AskDiamond@easysba.com is always available for specific questions regarding this or other SBA rules.