Economic Disadvantage Eligibility

SBA cannot determine if an individual is economically disadvantaged unless SBA has already found the individual to be socially disadvantaged. The individual majority owner(s) must prove both social disadvantage and economic disadvantage.

According to SBA's regulations, "economically disadvantaged individuals are socially disadvantaged individuals whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities."

To determine if an individual is also economically disadvantaged, each socially disadvantaged individual must provide the following to SBA:

- Narrative statement of economic disadvantage
- Personal financial information (including tax returns and certain SBA forms)
    - In every case, when married, the socially disadvantaged individual must submit separate financial information to SBA for his or her spouse (including tax returns and certain SBA forms).

Firms owned by an entity have different requirements and generally do not have to prove economic disadvantage for individual owners. Eligible entities are American Indians, Native Alaskans, Native Hawaiians and Certified Development Companies.

Factors SBA Considers to Determine Economic Disadvantage

In reviewing economic disadvantage, SBA reviews several factors to determine if a socially disadvantaged individual is economically disadvantaged: These factors include:

- All income for the past three years, including any unusual income levels
- Fair market value of all assets
- Personal net worth (assets and liabilities)
- Transfer of assets to an immediate family member, directly or via trust
- Availability of individual retirement account (IRA) funds or other official retirement accounts
- Income received from the firm when filing taxes as an S corporation or partnership
- Reinvestments into the applicant firm
- Tax payments for the firm

Majority Owner's Spouse's Role

In certain cases, SBA will consider a spouse's financial situation when determining whether the applicant is economically disadvantaged. SBA looks to the role of the spouse in the applicant firm. Particularly whether the spouse:

- has a role in the business
- has lent money to the firm
- provided credit support to the firm
- guaranteed a loan

In every case, when married, the socially disadvantaged individual must submit separate financial information to SBA for his or her spouse (including tax returns and certain SBA forms).

Separate economic disadvantaged eligibility requirements exist for a business that is owned by American Indians, Native Alaskans, Native Hawaiians and Certified Development Companies.

Economic Thresholds - Assets, Income, Net Worth

Before SBA can approve an application, the individuals claiming to be disadvantaged must submit supporting documents to prove their assets, income, and net worth fall below certain threshold amounts. These include:

- Assets cannot exceed $4 million
- Personal income cannot exceed $250,000, averaged over 3 years
- Net worth must be less than $250,000

To be sure the small business owners are not unfairly penalized, review how SBA calculates your assets, income, and net worth below.

How SBA calculates IRA or other retirement accounts: In certain circumstances, funds in an IRA or other retirement account may be excluded from SBA's calculation of assets and net worth. SBA recognizes that small business owners often use retirement savings as a vehicle to fund the business. For each application, SBA looks closely at these assets and might exclude them from the calculation of assets and net worth.

How SBA calculates home equity and business equity: In every instance, the individual's home equity and firm equity are excluded from SBA's calculation of net worth. SBA recognizes that small business owners often use home equity to fund the business. For every individual applicant, SBA excludes home equity in the calculation of net worth. Still, the full market value of the individual's home is counted as an Asset.

How SBA calculates S corporations or partnerships distributions: In certain instances, such distributions are excluded from SBA's calculation of personal income and net worth. SBA recognizes that small business owners often "pay themselves" to pay the firm's taxes, particularly when the firm files its taxes as an S corporation. When the individual applicant proves that such money was either reinvested in the firm or used to pay firm taxes, those distributions will not be counted as income nor an asset for net worth calculations.

How SBA calculates personal income: In every instance, SBA reviews income averaged over three years preceding submission of the application. SBA does not penalize small business owners for having one good year. Instead, we look to patterns and trends. To calculate income, SBA averages it over three years. This is why SBA requires full tax returns (including all schedules, attachments, and W-2s) for three years preceding the firm's application.

Source: www.sba.gov