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Busting the 'Free Money' Myth

Searching for a government grant or no-interest loan to start a business? Don't waste your time

by Kerry Miller

When Tina Washington first told people about her idea to open a kid's sports academy in Athens, Ga., she got a lot of encouragement. As an African-American female, she could look forward to gobs of money out there to help her start a business, friends said. Many advised her to inquire about grants, so Washington made an appointment at a local Small Business Development Center (SBDC), the Small Business Administration's largest small-business assistance program. It was there that a counselor broke the news: Those small-business grants and interest-free loans she'd been hearing so much about? They didn't exist.

"I've worked in small-business development since 1989 and there have never been any special programs for women and minorities in terms of easier access to money," says Lori Kravets, executive director of the Growth Opportunity Connection, a nonprofit entrepreneurship assistance center in Kansas City, Mo. The SBA does fund women's and minority business centers, but those provide technical assistance, not financing, and "they're no different from what anybody could get at a Small Business Development Center."

"If you think about it, it makes sense," Washington says. "If there was a whole bunch of free money out there, there wouldn't be a need for the SBDC." It was still a disappointing blow, however—and Washington is far from the first entrepreneur to experience such a setback.

"It's sort of a running joke among small-business assistance programs," says Allan Adams, state director of the Georgia SBDC. "The idea that there's just somebody standing around to give you \$100,000 and if you don't pay it back it's not a big deal? That's just not true," says Adams. "We spend a lot of time popping that bubble for people."

Still, the myth of abundant "free money" to start a small business has stubbornly defied debunking for decades. Like most myths it contains a kernel of truth—the U.S. government does give grants to assist small businesses. Of course, virtually all of that money flows to local governments, state agencies, and nonprofits—not individuals.

Too Good to be True

Many small-business counselors and lenders across the country lay the blame at the feet of one man: Matthew Lesko, a figure well-known to insomniacs with basic cable as "the question mark guy" for his signature suit. Since the 1980s Lesko has sold millions of copies of phonebook-sized books with titles like *Free Money for Entrepreneurs*.

"We can always tell when his infomercials are on television," says Jim Hammersley, the director of loan programs at the SBA—it's when the receptionist's phone starts ringing off the hook with callers determined to get some of that "free government money."

Since he helped create the Virginia Business Information Center in 2003, Will Vehrs at the Virginia Department of Business Assistance has fielded thousands of calls from grant-seeking entrepreneurs. "It's this sort of virus that spreads," Vehrs says. "Somebody says they're going to start a business, and then somebody else says, 'Oh, well, an uncle of mine started a business and he got a grant!'"

The reality of the situation can be a hard pill for callers to swallow. "A lot of people get agitated—they just know there's someone, somewhere who knows about these grants," Vehrs says. "You have to resist the temptation to say, 'You know, if there was free money out there, I would have grabbed it long before you called.'" At one point, Vehrs started offering \$100 to anyone who could provide proof of a grant received to start a small business. (He wasn't surprised when none of those apocryphal uncles showed up to claim their winnings.)

Lesko doesn't deny that when some people hear him talk about government grants they immediately assume they can be found at the SBA. "If they need somebody to blame, they can blame me," he says. "My problem is that in saying there are no grants, they imply there are none in the world, which is wrong."

SBA Loans Cost More

Entrepreneurs who aren't sidetracked searching for grants are often similarly disappointed to discover that, while the SBA does lend money, it doesn't hand out interest-free or low-interest loans to start new businesses. It's true that the disaster-recovery arm of the SBA makes federally subsidized loans to individuals and businesses affected by disasters, but the SBA's authority over this program is essentially a bureaucratic quirk. (Adding to the confusion: When interest rates were skyrocketing in the mid-1980s, a short-lived SBA direct-loan program did offer small-business loans at a fixed rate of 8%, "but we haven't had money for that for years," Hammersley says.)

In fact, because SBA loans are considered riskier, borrowers pay a slight premium for the small "credit enhancement" an SBA guarantee provides. Hammersley says the SBA avoids using the term "low interest" to describe its programs because, with the exception of disaster loans, SBA loans aren't intended to be below market rate. In most cases, borrowers with good enough credit to qualify for an SBA 7(a) loan could get a lower interest rate on a conventional bank loan, Adams says. "And if you've got bad credit and no collateral, chances are no one's going to lend you money."

Good Places to Start

Of course—as Lesko is quick to point out—there are exceptions. Some state and local economic development offices sponsor low-interest, revolving loan funds or microloan programs. The amounts disbursed are typically very small—\$5,000 or less—though a handful offer more. (In Minnesota, for example, entrepreneurs can qualify for state-subsidized loans up to \$300,000 to fund a business that will create jobs in low-income areas of the state.)

But entrepreneurs would be wise to think twice before forking over cash for books or workshops that promise to divulge the "secrets" of getting a grant or a loan. Adams says entrepreneurs would be a lot better off starting their funding search at a local SBDC office, or that of another SBA-funded program, such as SCORE. The answers won't be any different, he says. "If you'd have come to the SBDC we'd have told you for nothin'."

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