

SBA 504

CERTIFIED DEVELOPMENT COMPANY LOAN PROGRAM

The U.S. Small Business Administration (SBA) 504 loan program can provide long term fixed asset financing to eligible small businesses through its Certified Development Company Program for the acquisition, construction, expansion or renovation of land and buildings or purchase of long-life equipment.

HOW DOES IT WORK?

Certified Development Companies (CDC's) are certified by SBA to package, process, close and service the 504 loans. CDC's obtain loan funds by issuing debentures guaranteed by SBA and purchased by the Federal Financing Bank for sale to investors.

Basically, a CDC is a corporation that is formed with its chief purpose to promote and assist the growth and development of small businesses. It must be a nonprofit corporation with a minimum of 25 members with representation from local government, private lending institutions, community organization, and the business sector, including a five-person board of directors which meets bi-monthly. One private lender must be represented on the board. CDC's are authorized to sell debentures, with SBA's 100 percent guaranty, through a pool at public offering.

WHAT ARE THE TERMS?

Business borrower (or CDC) must provide a minimum of 10 percent of the project cost, except in cases of a new business (in operation for 2 years or less) or for single or limited purpose buildings, which would require an additional 5% equity requirement for either condition. A private financial institution must provide at least 50 percent of cost on a first mortgage basis. A certified development company will provide the other 40 percent through the sale of SBA guaranteed debentures.

New Business: 15% minimum equity requirement for businesses in operation for 2 years or less. The maximum SBA portion will be reduced to 35%. **Buyouts:** If the applicant purchases an existing business that has been in operation for 2 years or more, either by capital stock purchase or purchase of assets, the criteria for determining "new business" status would include continuity of the same management, product line and demographics of the business.

Funded in part through a cooperative agreement with the U.S. Small Business Administration. All opinions, conclusions or recommendations expressed are those of the author(s) and do not necessarily reflect the views of the SBA. Reasonable accommodations for persons with disabilities will be made if requested at least two weeks in advance. Contact NEAR SBDC, 225 Church Street, Huntsville, AL 35804 at 256-535-2061 to make arrangements.



An Institutional Member of the Alabama Small Business Development Consortium

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Single or limited purpose buildings: 15% minimum equity is required for single or limited purpose buildings or structures. The SBA portion will be reduced to 35%. **Definition:** "a limited market property with a unique physical design, special construction materials, or a layout that restricts its utility to the use for which it was built; also called special design property". Examples: gas stations, motels, car washes, marinas, bowling alleys, or any other facilities that would have limited markets or would require extraordinary costs to make them marketable.

Projects meeting both of the above conditions: 20% minimum equity is required for projects involving businesses that have been in business for 2 years or less which are constructing or acquiring a single or limited purpose building or structure. The maximum SBA portion will be reduced to 30%.

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INTEREST RATE

Bank sets interest rate on first mortgage portion (fixed or variable). SBA debenture note is based on the current average market yield on outstanding marketable U. S. obligations with comparable maturities at a fixed rate of interest.

Lender Participation Fee: The first mortgage lender will be required to pay SBA a one-time fee in amount equal to 50 basis points (1/2 of 1 percent) of the principal amount of the senior mortgage associated with the 504 loan.

TYPICAL PROJECT

<u>Source</u>	<u>% of Project</u>	<u>Term</u>	<u>Interest Rate</u>	<u>Collateral</u>
Bank conventional loan	50%	10 yrs.	Market Rate	First Mortgage
SBA guaranteed debenture	40%	10 or 20 yrs.	Fixed	Second Mortgage
Small business concern (or CDC)	10%			Third Mortgage (if CDC)

EXAMPLES:

	<u>\$200,000 Project</u>	<u>\$1,000,000 Project</u>	<u>\$2,000,000 Project</u>
Bank conventional loan	\$100,000 50%	\$500,000 50%	\$1,050,000 52.5%
SBA guaranteed debenture	\$ 80,000 40%	\$400,000 40%	\$ 750,000 37.5%
Small business concern (or CDC)	\$ 20,000 10%	\$100,000 10%	\$ 200,000 10.0%

MAXIMUM AMOUNT

Private sector first mortgage - no limit, but usually must be at least 50 percent of project cost.

SBA guaranteed debenture portion - \$1,000,000, limited to 40 percent of project cost. The borrower must provide at least 10 percent of project cost. SBA has established a guideline of creating at least one job for each \$35,000 debenture amount.

The maximum SBA guarantee is increased from \$1,000,000 to \$1.3 million for projects achieving a "Public Policy Goal."

THE PUBLIC POLICY GOALS AND REQUIREMENTS ARE:

- BUSINESS DISTRICT REVITALIZATION:** a project located within a business area of a community with a recognized revitalization or redevelopment plan that encourages business development as a means of enhancing the economic productivity of such area. A recognized plan is one that has been adopted by a local unit of government.
- EXPANSION OF EXPORTS:** a project in which the eligible small business concern (SBC) will retain or expand its ability to produce or sell its goods or services for purchase by buyers outside of the United States. To qualify, at least 10 percent of the SBC's revenue must be from export sales at the time of the project.

3. **RURAL DEVELOPMENT:** a project located in an area as defined in 13 CFR 108.2.
4. **ENHANCED ECONOMIC COMPETITION:** a project in which the SBC is engaged in advancement or technology, plant retooling (expansion or modernization of manufacturing facilities), conversion to robotics, or competition with imports.
5. **CHANGES NECESSITATED BY FEDERAL BUDGET CUTBACKS:** a project in which the SBC is locating or expanding in an area impacted by Federal budget cutbacks, such as facility closings or cutbacks in defense related industries.
6. **BUSINESS RESTRUCTURING ARISING FROM FEDERALLY MANDATED STANDARDS OR POLICIES:** affecting the environment or the safety and health of employees, such as requirements for pollution control equipment, removal/encapsulation of asbestos, etc.
7. **EXPANSION OF MINORITY BUSINESS DEVELOPMENT:** A small business concern which is at least 51% unconditionally owned by an individual(s) who is member of a designated group presumed by SBA to be socially disadvantaged.
8. **WOMEN-OWNED BUSINESS DEVELOPMENT:** A small business concern which is at least 51% unconditionally owned by a female.

COLLATERAL

Bank conventional loan is secured by a first mortgage on assets purchased or improved and must have at least a 10-year maturity. SBA debenture is secured by a second mortgage and the required personal guaranties of the owners.

ELIGIBLE BUSINESSES

For profit businesses with a net worth of less than \$6 million dollars and average net profit after taxes for the last two years not exceeding \$2 million dollars.

INELIGIBLE BUSINESSES

Non-profit corporations
 Financial institutions
 Real estate investment

INELIGIBLE USES

Working capital Venture capital
 Refinancing Inventory

HOW TO APPLY FOR A 504 LOAN

You should contact a CDC to initiate a 504 loan. They will assist the small business in packaging the loan application.

CDC'S IN ALABAMA

1. **ALACOM FINANCE**
 117 Southcrest Drive, Suite 100
 Homewood, Alabama 35209

Telephone: 205-942-3360
 Fax: 205-942-5984
 Toll-free 800-239-5909
 Contact: Diane D. Roehrig
 Diane McDonald

AREAS OF OPERATION

All counties in Alabama,
 excluding Washington,
 Choctaw & Sumter

2. Birmingham City Wide Jefferson & Shelby County Local Development Company
110 12th Street North
Birmingham, Alabama 35203

Telephone: 205-250-6380
Contact: Wayne Wisner

3. Greater Mobile Development Corporation Mobile and Baldwin Counties
P.O. Box 1827
Mobile, Alabama 36633

Telephone: 334-434-7591
Contact: Teresa Sands

4. Southern Development Council All counties in Alabama
8132 Old Federal Road
Montgomery, Alabama 36117-8007

Telephone: 334-244-1801
800-499-3034
Fax: 334-244-1421

Contact: John Reynolds
Everette Strong
Angie Winter

FEES ASSOCIATED WITH THE PROGRAM

ONE TIME FEE

- (A) Loan Packaging Fee - This is 1.5 percent of the 40 percent portion. This fee is wired directly to the CDC when the debenture sells.
- (B) Reserve Account - When the debenture sells, a reserve account is set up. This is estimated at .5 percent of the 40 percent portion.
- (C) Funding Fee - .25 of 1 percent to cover other cost associated with selling the debenture.
- (D) Legal Closing Cost - This is an estimate of the attorney's fees for closing the SBA debenture loan only.
- (E) Underwriting Fee - .625 of 1 percent SBA share of project cost plus "A" through "D" above.

SERVICING FEE

These fees are added to the interest rate and is the difference between the debenture and the final rate.

Colson Services Corporation receives .125 of 1 percent per year on the outstanding balance for the first 5 years, then it is .0625 of 1 percent per year on the outstanding balance.

The CDC receives .5 of 1 percent per year on the outstanding balance.

LOAN CLOSING FEE

When the loan closes, the bank portion of the loan is closed at the same time as the CDC closing. The loan closing

fees should be computed on the basis of actual hours devoted to the project cost, per the attorney's hourly rate for the type work performed.

Interim interest, appraisal fees, architect fees, etc. are included in contingencies. Loan closing fee, packaging fee, reserve account, etc. are added directly to the SBA portion of the loan. The servicing fees are added directly to the interest rate of the debenture.

SAMPLE

Project Cost	\$125,000.00	(Land \$30,000, construction \$92,000, contingencies \$3,000)
Bank Portion	62,500.00	(50%)
SBA Portion	50,000.00	(40%)
CDC or SBC Injection	<u>12,500.00</u>	(10%)
	\$125,000.00	

PRICING THE DEBENTURE

(A) SBA Share (40%) of Project Cost	\$50,000.00
(B) Administrative Costs	
1. Reserve Amount (Ax0.005)	250.00
2. Funding Fee (Ax0.0025)	125.00
3. CDC Processing Fee (Ax0.015)	750.00
4. Closing Costs	1,000.00
5. Total (B.1.thru B.4.)	2,125.00
6. Underwriters Fee	331.25
7. Total (B.5.+ B.6.)	<u>2,456.25</u>
(C) Total Debenture Amount (A.+ B.7., rounded up to next thousand)	\$53,000.00