SBA LOANS A PLEASANT SURPRISE

There are not too many government programs that actually impress me. Often described as vastly underutilized, the U.S. Small Business Administration was established in 1953 as an independent agency of the Federal government. Its purpose was a noble one…to help Americans start, build and grow businesses. During the economic downturn in the past few years, the SBA programs have been a Godsend to the commercial real estate business, providing a financing source when conventional lenders all but disappeared from the scene.

Two different programs make up the guts of the SBA effort to assist small businesses. The most popular program , called the 7(a), works by providing guarantees to private sector lenders who secure financing for small businesses. What's weird about this SBA form of financing is that the SBA is not actually lending money directly. It is structured to make it less risky for a local lender to provide you with the financing you need. If the borrower fails to repay their obligation and a payment default occurs, the SBA will reimburse the lender for up to 75% of the loss. What lender wouldn't make a sensible loan with a guarantee like that?

The 7(a) loan funds can be used to 1) buy owner occupied commercial real estate, 2) start a new business , 3) purchase or expand an existing business, 4) buy machinery and equipment, 5) augment working capital, 6) refinance debt and balloon payments, 7) start a franchise, 8) make leasehold improvements, 9) remodel or renovate, 10) increase inventory. In most cases banks will want 2-3 years of financial statements and tax returns and most will want 10-20% owner's equity (downpayment) in the purchase so that there is "skin in the game" by the borrower. Interest rates have been relatively low in 2019. Amortization periods are up to 20 years and loans can be fixed or variable. Other parameters exist but this type of loan is one you should definitely explore if you are in the market.

The other program known as the SBA 504 program is a co-lending product between a private sector lender and what is known as a Certified Development Company (CDC). There are about 270 CDC's nationwide, each operating in a specific geographic area. The typical 504 project requires only 10% equity (downpayment) from the borrower which is quite low in modern lending practices. The balance of the loan is split between a private sector lender (50%) and the CDC (40%). The private sector lender portion (50%) is 100% backed (guaranteed) by an SBA debenture (bond). 504 loans are funded by the sale of bonds which are packaged and sold on Wall Street. So there are actually two loans being made to the borrower with a 504, one from the bank and one from the CDC. The bank gets a 50% loan to value first lien position on the assets being purchased thereby cutting its risk in half! The CDC provides the next 40% in a second lien position. The 504 has a more limited scope than the 7(a) and is typically used to purchase existing owner occupied (51% or more) commercial/industrial buildings, but they can also be used for purchase of land and construction of new facilities. Modernizing, converting or renovating existing facilities also qualifies as does purchase of long term machinery and equipment.

The benefits of the 504 loan are said to be: 1) low downpayment (more people can afford to buy!), 2) below market fixed rate interest rate, 3) long term financing (no 3-5 year balloons), 4) loan fees may be financed , 5) assumable loan 6) up to 25 year amortization periods, 7) can be used to refinance any existing loan.

We have recommended both of these programs to a number of our clients over the years and the results have been gratifying for all. The old myths of SBA loans being only for low income, disadvantaged or minorities are invalid so these programs have wide appeal and applicability. Furthermore, the time it takes to process these loans has been streamlined significantly so transactions can go from contract to closing in 60-75 days. In addition, we are seeing fixed commercial interest rates as low as 4.74%!

If any of this sounds appealing, let me put you in touch with a lender or CDC and get the process started. It costs nothing to get you pre-qualified.

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