

# DELVAL BUSINESS FINANCE CORP.

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## SBA 504 Loan Program - Fact Sheet

**Introduction – DELVAL BUSINESS FINANCE CORP.** (DELVAL) is a private non-profit corporation that is licensed by the U.S. Small Business Administration ("SBA") to make SBA 504 loans to businesses throughout the State of Pennsylvania and New Castle County, Delaware. DelVal's role is to market the 504 program, assist banks to screen and structure eligible projects, prepare the loan packages, negotiate with SBA, coordinate the closing, and service the loans after they are funded.

**Loan Program** - The SBA 504 Loan program provides businesses with long-term, below-market, fixed-rate, subordinated loans to purchase real estate, build, expand, renovate or make leasehold improvements to buildings, or purchase machinery and equipment. The program requires only a small cash down-payment thereby preserving the business's working capital. The purpose of the 504 loan program is to create or retain jobs in growing small and mid-sized firms.

**Eligible Businesses** - In order to be eligible for 504 financing a business must be a for-profit corporation, partnership or proprietorship, its net worth must not exceed \$ 7.5 million, and its average net income after taxes for the preceding two year must not exceed \$2.5 million.

**Ineligible Businesses** - Businesses that are ineligible for 504 financing include non-profit organizations, investment companies, lending institutions, real estate development companies, and unregulated media firms.

**Financing Structure - DELVAL** provides 504 financing by issuing an SBA-guaranteed debenture for up to 40% of the total cost of a project. A commercial lender selected by the borrower (or referred by DelVal) provides financing for at least 50% of the project. The borrower provides the remaining 10% in the form of equity or subordinated debt. For new businesses and some special purpose buildings, the minimum investment from the borrower increases to 15% or 20%.

**Maximum Loan Amount** - The maximum amount of 504 financing which DelVal can provide is \$1,500,000 (up to \$2.0 million for exporters, minority-owned businesses, and businesses in rural areas or targeted business districts and up to \$ 4 million for manufactures.) and the minimum is \$100,000. There are no restrictions on the total project size - which has on some occasions exceeded \$ 10-12 million.

**Eligible Use of Proceeds** - Proceeds of the financing package may be used for the purchase of land; purchase or construction (or renovation) of a building; modernization, renovation, including leasehold improvements; purchase of machinery and equipment [minimum useful life of ten (10) years]; and the related soft costs such as construction period interest and professional fees for accountants, engineers, lawyers, appraisers, etc.

**Ineligible Uses of Proceeds** - The 504 program financing may not be used for working capital, refinancing of existing debt, or to acquire property for purely investment purposes.

**Term** - Machinery and equipment may be financed with ten (10) year 504 debentures and real estate with twenty (20) year debentures. A minimum of seven (7) year financing is required from the commercial lender for machinery and equipment and ten (10) years for real estate.

**Interest Rate and Fees** - The interest rate on the 504 financing is fixed and is based on the prevailing rates for five (5) and ten (10) year U.S. Treasury issues (for ten and twenty year 504 loans respectively), plus a spread of approximately 2.5%. SBA, DelVal and Colson Servicing Corp. receive fees for processing the loan requests and servicing the loans after

they are disbursed. However, these fees are included in the spread over Treasury rates, and the effective rates for the borrowers as of 12/1/2006 is about 6%. The rates are set when the acquisition and/or construction is completed and the SBA pays off the private lender's interim financing.

**Bank Financing** - A bank or commercial lender provides a first mortgage at market terms and conditions and provides interim financing on the SBA portion of the project until the acquisition or construction is completed and the paperwork is finalized. At that time DelVal's attorney coordinates the SBA closing, and after the documentation is completed, the bank receives a wire-transfer for the SBA portion of the project. The private lender is required to pay the SBA a one time fee of one-half of one percent (0.5%) of the amount of its first mortgage, which at the lender's option may be passed on to their borrower.

**Deposits - DelVal** requires a deposit prior to submitting to SBA which is returned in part if the Section 504 loan is not approved by the SBA. The balance of DelVal's fee is payable in part when the SBA authorization letter is received by the borrower and with the balance due at the final funding of SBA's portion of the financing.

**Collateral** - Collateral is usually limited to a second lien on the fixed assets being financed. The commercial lender has the security of a first lien on the assets financed.

**Personal Guarantees** - Personal guarantees are required of those persons owning 20% or more of the business or the property financed with the Section 504 loan.

**Repayment** - SBA 504 loan repayment begins on the first day of the month following SBA's funding. SBA 504 loans are self-amortizing with level monthly repayments.

**Legal Costs** - The small business borrower is responsible for all legal costs associated with the 504 financing including the attorney for DelVal who closes the loan for a fee of approximately \$3,000 plus out-of-pocket costs.

**Prepayments** - A prepayment premium is required of 100% of the borrower's interest rate the first year, and declining 10% per year then-after for 20 year loans and declining 20% per year then-after for 10 year loans, however because of the advantageous terms, few 504 loans are prepaid. The prepayment premium occurs only in the first ten years of a 20 year loan, and only in the first five years of a 10 year loan.

**Other** - The business must occupy at least 51% of the building being purchased or renovated immediately upon acquisition and/or completion of renovations. If constructing a new building, the business must occupy at least 60% of the space upon completion of construction and may lease out the remaining 40%.

**Benefits to Business Borrowers** - The benefits to business borrowers of using the SBA 504 loan program include low cash down payment (typically 10% of fixed assets and related soft costs), fixed-interest rate (for the 504 portion of the project), and lower interest rates (in comparison with equity or other subordinated debt sources). When soft costs like professional fees and interim interest are included, the borrower's cash may be as low as 5% of the hard project costs.

**Benefits to Lenders** - The benefits to banks and commercial lenders from using the SBA 504 program include lower loan-to-value, better cash flow coverage for the borrower through the availability of long term fixed-rate financing for the borrower and CRA credits for working with DelVal and providing at least 10 year financing on the first mortgage..

<b>Sample -</b>	<u>Uses of Funds</u>		<u>Sources of Funds</u>	
	Purchase property	\$750,000	Commercial lender	\$ 500,000 - 50% 1 <sup>st</sup> mortgage
	Construction/renovation	200,000	SBA 504/Delval	400,000 - 40% 2 <sup>nd</sup> mortgage
	Closing costs/other	<u>50,000</u>	Small business	<u>100,000</u> - 10% Equity
	Total	\$1,000,000	Total	\$ 1,000,000

**How to Proceed** - Please call Michael Schwartz, President at 717-420-5925 or e-mail at [mschwartz@delval504.com](mailto:mschwartz@delval504.com) to discuss SBA Section 504 financing.