

# Minnesota Business Finance Corporation

- Certified Development Company
- Licensed and regulated by the SBA
- 501(c)(3) Nonprofit corporation
- Provides small-business owners with fixed-asset financing
- Promotes economic growth in the community

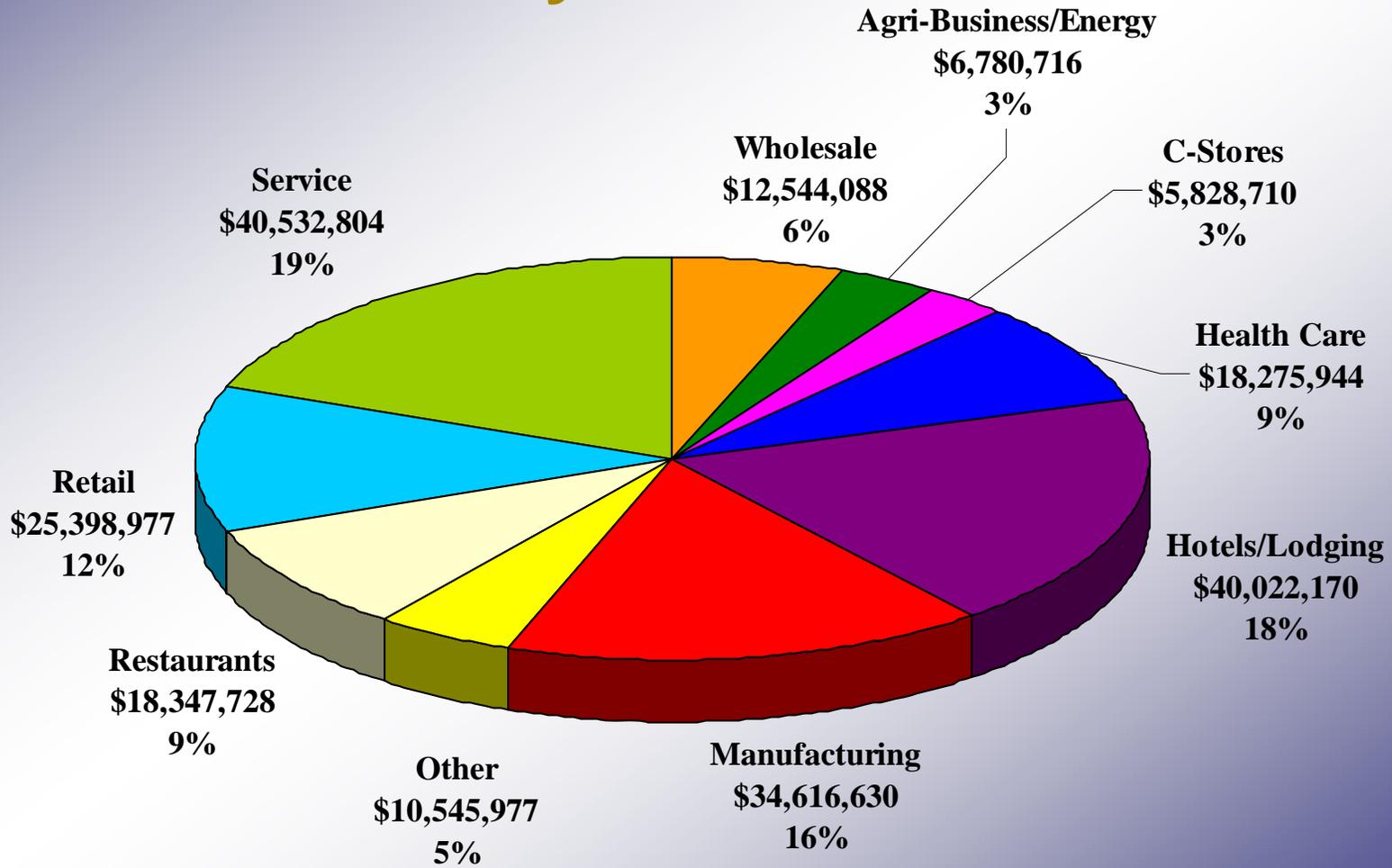
# **MBFC 504 Loan Approvals FY2009**

**(10-01-08 to 09-30-09)**

- Loans Approved 64
- Total Debenture \$ 28,256,000
- Total Project Cost \$ 78,482,083

# MBFC 504 Loan Portfolio (\$212.9 MM)

## Industry Diversification



# Benefits of 504 Loan

## Borrower

- Lower equity injection (10 to 20%)
- 10- and 20-year fixed interest rates
- Short-term assets remain lien-free to support other financing needs
- 10-year (equipment) and 20-year (real estate) maturities

# Benefits of 504 Loan

## Third-Party Lender

- Risk management tool
- Excellent loan-to-value (typically 50% or less)
- Senior lien position
- Pricing flexibility on first mortgage portion
- First mortgage portion may be sold on secondary market
- Alleviates legal lending limit concerns
- Community Reinvestment Act credit

# American Recovery and Reinvestment Act of 2009

- Signed into law by President Obama February 17, 2009
- Provides \$730 million to SBA, of which \$375 million is used for temporary fee reductions on SBA loans. Makes changes to the agency's lending and investment programs

# 504 Fee Reduction

- Temporary elimination of the bank participation fee (currently 0.5% of bank's permanent note.)
- Temporary elimination of the CDC processing fee paid by the borrower (currently 1.5% of the net debenture.)
- Effective on loans approved by SBA on or after February 17, 2009.
- Expiration date is 9/30/2010 or when appropriated funds are exhausted.

# Effect of Fee Reduction

## Project Examples

	<b><i>\$1,000,000 Project</i></b>	<b><i>\$4,000,000 Project</i></b>
<b>Lender</b>	\$500,000	\$2,000,000
<b>SBA 504</b>	\$400,000	\$1,600,000
<b>Equity</b>	\$100,000	\$400,000
<b>CDC Processing Fee</b>	\$6,000	\$24,000
<b>Third Party Lender Fee</b>	\$2,500	\$10,000
<b>Total Fees Eliminated</b>	\$8,500	\$34,000

# Debenture/Project Size

## Debenture size

- Most projects: \$1.5 to \$2 million
- Manufacturing: \$4 million
- Reducing energy use by 10%: \$4 million
- Renewable Energy Production: \$4 million
- Sustainable Design: \$2 million

## Project size

- \$250,000 minimum no maximum

# Eligible Project Costs

- Land acquisition
- Site improvements
- Purchase of existing building(s)
- Remodeling, expanding, or renovating existing building(s)
- Construction of new buildings
- Acquisition of machinery and equipment
- Limited Debt Refinance – See specific rules
- Contingency reserve for cost overruns ( $\leq 10\%$ )
- Professional fees
- Repayment of interim financing, points, origination fee, interest

# Ineligible Project Costs

- Working capital
- Counseling or management services fees
- Incorporation or other organizational costs
- Commitment, broker & origination fees for third-party permanent loan
- Franchise fees
- Equipment/furnishings < 10-year useful life
- Automobiles, trucks, airplanes
- Advertising
- Closing legal fees
- Goodwill and other intangibles

# Debt Refinancing

- Limited debt refinancing as an eligible 504 Project Cost is a permanent change to the 504 Loan Program.
- The 504 Project must involve expansion of a small business
  - “Expansion” is broadly defined to include any Project that involves the acquisition, construction or improvement of land, building or equipment for use by the small business.

# Amount of Debt That Can Be Refinanced

- Any amount of existing debt that does not exceed 50% of the cost of expansion may be refinanced as long as following conditions are met:
  - The existing debt was used for 504-eligible assets: to acquire land, including a building, construct a building or the purchase equipment.
  - The existing debt was incurred for the benefit of the small business.
  - The existing debt is collateralized by the fixed assets.
  - The refinancing will provide a substantial benefit to Borrower – new installment amount will be at least 10% less than the existing payment amount.

# Conditions of Refinance *cont.*

- Borrower has been current on all payments on the existing debt for not less than 1 year preceding the date of refinancing.
- The refinancing will provide better terms or rate of interest than the existing debt on the date of refinancing.
- The 504 Loan proceeds are not used to refinance debt owed to:
  - An Associate of the 504 Loan applicant
  - An SBIC
  - Any creditor in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from the existing debt.

# Occupancy

## Existing building

- Borrower and operating company (OC) must occupy at least 51% initially
- Borrower and OC may lease out up to 49% of additional rentable property indefinitely

## New construction

- Must occupy at least 60% of rentable property
- May lease out up to 20% of rentable property indefinitely
- Must occupy some of remaining space within three years, all remaining unleased space within 10 years

# Basic 504 Loan Structure

## Financing/Equity Requirements

- Third-party lender provides 50%
- CDC/SBA provides 40%
- Borrower provides 10% owners' equity

## Factors impacting owners' equity

- Start-ups = 15%
- Special-purpose real estate = 15%
- Both start-up and special purpose RE = 20%

# What Qualifies as Borrower Contribution?

- Cash
- Eligible land contribution, including buildings, structures and site improvements which will be part of project property
- Funds may be borrowed or received from other sources

# Loan Structure Standard

## 50/40/10

- Existing business
- No special-purpose real estate
- Good credit risk
- Project cost = \$1,000,000

Third Party Lender	First Mortgage	\$ 500,000	50%
SBA	Second Mortgage	\$ 400,000	40%
Borrower Cash Contribution		<u>\$ 100,000*</u>	10%
		\$1,000,000	

\* may include gap financing

# 50/30/20 Loan Structure

## Start-Up and Special-Purpose Facility

- Start-up = 5% additional contribution needed
- Special-purpose real estate = 5% additional needed
- Project cost = \$1,000,000
- Inventory/working capital = \$30,000 needed

		<u>504 Loan</u>	<u>Other</u>
Third-Party Lender	First Mortgage	\$ 500,000	
SBA	Second Mortgage	\$ 300,000	
Borrower Contribution		\$ <u>200,000*</u>	<u>30,000</u>
		\$1,000,000	\$30,000

\* may include gap financing

# Sample 504 Loan Structure

“Grossing Up”

- Borrower wants to utilize existing land/building equity for all or part of contribution, seeks financing for up to 100% of project costs
- Project cost = \$1,000,000
- Grossed up = \$1,111,111 ( $\$1,000,000/90\%$  LTV)

<u>Typical 50/40/10</u>		<u>Grossed-Up 50/40/10</u>
\$500,000	Third-Party Lender	\$555,556
\$400,000	SBA	\$444,444
<u>\$100,000</u>	Borrower Contribution	<u>\$111,111</u>
\$1,000,000		\$1,111,111

# Loan Process

- Call/visit with MBFC staff
- Prepare application
- MBFC loan approval
- SBA loan approval
- SBA issues authorization/loan agreement
- Project completed and loan funds disbursed by bank
- SBA 504 loan closing
- Debenture sells – SBA 504 loan funds