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Businesses Find Cheap Capital in SBA Mortgages

By COLLEEN DEBAISE

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FOR YEARS, A LITTLE-KNOWN Small Business Administration lending program known as the 504 has stood in the shadows of the agency's flagship loan program, the 7(a).

But now, as banks tighten their lending practices and commercial office space becomes cheaper in some markets, a growing number of business owners are turning to 504 loans. These loans can be used to purchase business real estate or fixed assets (such as heavy equipment or machinery). And, because 504s are backed by the government, they're typically easier and cheaper to secure than conventional commercial mortgages.

Here's how a 504 loan works. A small business decides to purchase, say, a commercial office building for \$1 million, which includes renovation work plus "soft" costs such as permit and design fees. To finance the purchase through a 504, the borrower must put down at least 10%, while an SBA-certified nonprofit agency lends another 40% through a government-backed bond offering. Then, a commercial bank or other lender provides the remaining 50%. Typically, the money is loaned at below-market interest rates, for longer terms than most commercial mortgages (say, a 20-year term rather than a 15-year term), making it more affordable for the average small-business owner.

The 504 "is a product that has so many advantages that it sells itself," says Roslyn Goldmacher, president of the nonprofit [Greater New York Development Co.](#), a Bethpage, N.Y., certified development company, or CDC, that specializes in 504 loans. "The biggest issue is awareness." The 504 is more complex than most conventional loans and therefore isn't well-marketed, she explains. And historically, many lenders have veered away from the 504 just to avoid all of the extra rules and steps (such as finding a partner CDC) involved.

But things are starting to change. "I would certainly say there's a lot more players now than there were three years ago, [when] we were one of the only banks that were pursuing this aggressively," says Laura Larson, SBA program manager with KeyBank in Cleveland. Now, with the economy unsteady, banks are more interested in making low-risk loans such as the 504, which is secured by the property and government bond, she says.

KeyBank recently worked with a number of small-business clients — including a boat-repair company, a printer and a heating/cooling company — that used 504 loans to buy buildings and equipment that they would have had to lease under other circumstances. Other big banks that provide 504 loans include Citibank, Bank of America and Chase.

A number of private lenders are providing 504 loans, too. "Our business is having the best year we've ever had," says Chris Hurn, founder of [Mercantile Commercial Capital](#), an Altamonte Springs, Fla., mortgage lender that helps a broad range of clients — including hotels, restaurants, professional-services firms and even doggie day-care operators — secure 504 loans. "I've often said it's the best-kept secret of the SBA."

While the 504 program's rules and restrictions might scare off some business owners, most businesses easily qualify, Hurn says. For example, because the 504 program is chiefly designed to encourage economic development, borrowers are expected to create or retain one job for every \$50,000 provided by the SBA. A business that doesn't meet that requirement, however, still might be able to qualify if it meets one of the program's community development goals, say, if the business is owned by a woman, minority or veteran. For more on 504 program rules, [click here](#).

And while a traditional commercial mortgage usually requires a business to put down a higher down payment (often, at least 20%) and pay soft costs out-of-pocket. The 504, on the other hand, provides for 90% financing of total costs. And thanks to lower rates and extended terms, "it's the least expensive capital available to small to midsize business owners right now," he says.

Another bonus: Unlike other SBA products, a business owner doesn't have to prove they've been turned down by a bank in order to qualify for the 504, says KeyBank's Larson. "Some savvy business owners who could be eligible for conventional financing might look at the 504 as a way to preserve cash," she says.

Small-business owners interested in a 504 should contact their bank or private lender, or their local CDC (there are about 300 nationwide). Keep in mind, the most appropriate candidates aren't start-ups, but rather businesses that are ready to buy commercial space because they "have weathered the cycles a bit," Hurn says.

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