
Ocean State Business Development Authority, Inc. is a Certified Development Company, licensed and regulated by the US Small Business Administration (SBA) (a federal agency) to make 504 loans in a specific geographic area. OSBDA serves the entire state of Rhode Island as well as contiguous areas in Connecticut and Massachusetts and has been providing 504 loans to borrowers since 1980. OSBDA's role is to help small businesses access long-term fixed-asset financing in partnership with the private sector, usually a financial institution. OSBDA processes, closes and services the loans.

- Most for-profit businesses with less than \$7.5 million in Net Worth or after tax profits of less than \$2.5 Million.

Permitted Use of Proceeds

- Acquisition of fixed assets such as land and buildings
- Purchase an existing building and make necessary renovations (this could be the building in which the small business currently operates)
- New construction or renovation
- Construct or remodel buildings on leased land (where the lease is longer than the term of the 504 loan). Outside collateral will generally be required.
- Acquire and install machinery and equipment with a minimum 10-year economic life.
- Professional costs (excluding legal fees)
- Refinancing is not permitted except to take out financing on property acquired within the last 9 months with interim funds

Economic Development Requirements

The 504 is a loan program designed to help small businesses expand and to promote economic development, therefore the SBA requires that projects financed by the program result in the creation or saving of jobs, at a certain ratio of jobs to dollars of the SBA's guaranty.

At this time, one job must be saved or created, within two years of project completion, for each \$50,000 in 504 funds or meeting other economic development goals such as:

- Manufacturers (SIC codes 20-49)
- Exporters (10% or more of sales)
- Minority-owned businesses (51% or more)
- Project in state-designated enterprise zones, empowerment zones and enterprise communities or areas with written redevelopment plans
- Change necessitated by federal budget cutbacks
- Increase productivity & competitiveness (retooling, robotics or modernization)
- Expand woman-owned business development
- Expand veteran-owned business development
- Projects which will provide significant community benefit (economic diversification or stabilization, stimulating other business development, or bringing new income into the community), which can be demonstrated by letters of support from community officials
- Assist businesses in a labor surplus area

OCEAN STATE BUSINESS DEVELOPMENT AUTHORITY, INC.

JOBS/INVESTMENT:

other economic development goals.

**INTEREST RATE &
TERMS OF LOAN:**

The rate is determined by market at the sale of participation in a pool of government securities. The rate is fixed for the term of the OSBDA/SBA loan. The rule of thumb in projecting a rate is: 10-year Treasury rates plus 225 basis points. Maturities of ten and twenty years are available on the 504 debenture, depending on the useful life of assets and the term of the private Job creation; one per \$50,000 in 504 funds or meeting lending participation.

**ELIGIBLE COLLATERAL/
SECURITY:**

Second mortgage and/or lien on assets purchased with proceeds of 504 loan. OSBDA may, at its discretion, look to collateral outside of the project when it is deemed necessary and appropriate.

BENEFITS:

Long term below market fixed rate financing. Equity requirement of 10% or more per Borrowers effectuating enhancement of working capital and stabilization of cash flow.

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Are You A Small Business... Looking to Expand? Look Into an SBA 504 Loan

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A few benefits of SBA 504 Loans...

Found that perfect building, but your banker says you need 30% down? Can't afford 30%? Plus pay for renovations and soft costs and still have enough working capital left over for the expansion? Well, a 504 certified development company can help you by making you a loan to buy that building through the SBA 504 loan program. Only 10%* down by you. All project costs are included-land, building, renovation and soft costs. The loans are long term and provide a low fixed interest rate. The SBA 504 loan program can even finance the machinery you need to buy. Interested?

***Please Note:** Equity of 15-20% is required for start-ups and businesses with irregular profitability, lack of historical debt service ability, a short track record or for single purpose properties.

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- You often need only **10%* down**
- Lets you keep more of your cash for working capital during your expansion
- Long term -- low fixed interest rate
- Finance your soft costs including accountant fees, title, insurance, attorney closing fees, etc.

The Role of the Certified Development Company

Certified Development Companies (CDC's) are regional economic development organizations that are licensed by the U.S. Small Business Administration (SBA). CDC's each have a geographic territory covering one or more counties. To see a listing of CDC's in your area, [click here](#) for our CDC Member Directory. CDC's make loans under the SBA 504 loan program

to assist small business. The CDC processes, approves, closes and services the loans. Funding is arranged by the CDC issuing a bond, and in all ways, the CDC is the direct lender for the SBA 504 loan program.

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Eligibility for SBA 504 Loans

- Organized as a for-profit business. The only not-for-profit companies eligible for SBA 504 loans are sheltered workshops.
- Legal entity-corporation, partnership, sole proprietor, limited liability company.
- any type of legitimate business- manufacturing, wholesale, service, professional service or retail.
- Located in or planning to locate in any area of the United States.
- Small business - either: net worth under \$7 million & net profits after taxes under \$2.5 million or meet SBA's other size standards (by sales or number of employees depending on NAICS code).
- Planning to use the loan proceeds for capital investment (land, building, leasehold improvements, renovation, construction, machinery & associated soft costs). The SBA 504 loan program is not a working capital program. See uses of loan proceeds section for more details.
- Another lender must be willing to participate in the financing. The SBA 504 loan finances up to 40% of the total project cost and the other lender finances 50%. The business or its owner typically puts in 10%. Economic development goals must be achieved through the project being financed. See section on economic development requirements.
- Owner-user of the project being financed (51% occupancy if existing building; 60% occupancy if new construction) Two or more unrelated small businesses may receive a 504 loan to buy or construct a building as long as they, together, will occupy at least 51% an existing building or 60% of new construction.

Companies that are **not** eligible for SBA 504 loans are: not-for-profit businesses (except sheltered workshops); businesses engaged in lending (such as banks, finance companies); passive holders of real estate and/or personal property; life insurance companies -- however an insurance agency is eligible;) businesses located in a foreign country or owned by aliens; businesses selling through a pyramid plan; illegal businesses; businesses which restrict patronage; government owned entities (excluding Native American Tribes); businesses engaged in promoting religion; consumer and marketing cooperatives (producer cooperatives are eligible); businesses engaged in loan packaging; businesses owned by persons of poor character; equity interest by lender, CDC or associates in applicant concern; businesses providing prurient sexual material; businesses that have previously defaulted on a Federal loan; businesses engaged in political or lobbying activities; and speculative businesses.

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What are the Permitted Uses of 504 Loan Proceeds?

- Acquisition of vacant land for construction of a building
- Acquisition of land and building

- Leasehold improvements
- Renovation of building; addition to building
- Construction of a building
- Acquisition of a commercial fishing vessel or party boat
- Acquisition of heavy duty machinery & equipment (such as printing press)
- Associated soft costs: title searches & insurance; attorneys fees; appraisals; environmental reports; architects; permits; surveys; installation of machinery; points on bridge loans, small amount of furniture and fixtures, etc.
- Not permitted are mortgage broker fees; points on permanent financing; moving expenses.
- Refinancing is not permitted except to take out financing on property acquired within last 9 months with interim funds.

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Economic Development Requirements

SBA 504 is a community lending program designed to improve the locality. Eligibility requires either:

1) Job creation or retention (one job per every \$50,000 borrowed from CDC under SBA 504)

OR

2) One of the following public policy goals to:

- Revitalize a business district of a community with a written revitalization or development plan
- Expand exports
- Expand minority business development (owned 51% or more by minority business person)
- Change necessitated by federal budget cutbacks
- Change required by mandated standard re health, safety, environment
- Increase productivity & competitiveness (retooling, robotics, or modernization)
- Expand woman-owned business development
- Expand veteran-owned business development

One of the following community development goals to:

- Help to improve, diversify or stabilize the economy of the locality
- Stimulate other business development in the community
- Bring new income into the community
- Assist manufacturing firms
- Assist businesses in a labor surplus area.

SBA 504 is not a real estate investment tool. It exists to help the community by helping small business have an impact on the community-by

creating jobs or in other ways benefiting the community.

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Deal Structure -- Financing

You determine the total project cost (hard and soft costs). A bank or other financial institution finances 50% of the cost and takes a first mortgage (lien) position on the assets financed. The CDC, through the SBA 504, finances 40% of the project cost up to a cap and takes a second mortgage position. You can put in as little as 10% equity.

Typical Project:

Cost

Acquisition of building	\$800,000
Renovations	\$100,000
Machinery	\$50,000
Soft costs	\$50,000
Total	\$1,000,000

Financing

Bank - first mortgage	\$500,000 permanent loan
SBA 504 - second mortgage	\$400,000 permanent loan
Equity	\$100,000
Total	\$1,000,000

Note: the seller can provide the 50% permanent financing but, under current regulations, the seller must be co-equal to or subordinate to the SBA 504 loan. The 50% can come from a variety of nonfederal sources such as banks, nonbank institutions, government agencies.

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Amount of 504 Loan

The CDC can lend you up to 40% of the project cost with a dollar cap of \$1,000,000. CDC can exceed \$1,000,000 and go up to \$1,300,000 of SBA 504 financing under the following conditions:

- the project will help revitalize a business community with a written revitalization plan or
- the project will help your company to expand its exporting or
- your company is 51% or more minority, woman or veteran owned or
- you are locating in a rural area or
- the project will increase productivity and competitiveness by retooling, modernization or assistance in competing with imports or
- your business was affected by federal budget cutbacks (such as defense downsizing).

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Rates and Terms

The rate on the SBA 504 portion is set when the CDC sells the bond to fund your loan. The rate is then fixed for the loan term. 504 bonds are amortized securities. For comparable rates, look at treasury rates. The SBA 504 rates can be found in the About DCFC Section of this web site. The effective rate (APR) will include program fees and a loan loss subsidy.

Loans are ten or twenty years; self liquidating. In order for the CDC to do a 20-year loan, the lender doing the 50% permanent first mortgage must have at least a ten year term. That lender can have a longer payout. Typically, lenders will lend with a 15-20 year term and 20-year payout. For a CDC to do a ten-year loan, the 50% lender must have a term of at least 7 years. Many lenders will match CDC's ten year term.

Principals (owners)

Owners must be US citizens or registered aliens with green card.

Owners cannot be convicted felons currently on probation.

Anyone who owns 20% or more of the operating company must personally guarantee (unsecured general guarantee).

Liquid assets of the principals are taken into account in determining eligibility. Too much liquid assets owned by a principal could disqualify the loan because it will be deemed that the project could be financed by the principal without SBA 504 assistance.

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Collateral

The CDC takes a subordinate (second mortgage) to secure its 40% portion of the financing, and the CDC takes a security interest in assets financed. Key Man life insurance is generally not required unless there is no succession of management. Should you need information on insurance visit the [504 Easy Term Life Insurance Center](#). Other assets of the business or principals are generally not required. (unless the company is a startup or the credit is unusually risky or the asset being financed is considered a single purpose asset or doesn't appraise high enough).

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Fees and Payments

All of the fees on the SBA 504 loan are added to the loan amount so that you can amortize their cost over the loan term. You will sign a note for the 40% of project cost plus the fees. Fees are based on the 40% of project cost: 1.5% of the 40% goes to CDC as its processing fee; .5% of the 40% is a reserve deposit; 1/4 of 1% of the 40% is a funding fee; loan loss coverage fee; various closing costs will be included; an amount for CDCs title insurance and recording fees can be added to the loan. In addition, when the loan closes, your monthly payment will include servicing fees based on the declining balance of the SBA 504 loan: 7/8% to CDC; 1/8% to SBA; 1/10% to central servicing agent.

Payments on the SBA 504 loan are made by ACH debit to the borrowers designated checking account on the first of each month after the loan closes. Payments on the 504 loan are separate from your payments on the 50% first mortgage loan.

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Special Notes

There is a prepayment penalty for the first half of the loan term on the SBA 504 loan. In start up situations or single purpose buildings being financed, an equity injection of 15% is required.

The Certified Lender is a permanent lender only. This means the 50% first mortgage lender will have to bridge the Certified Lender's 504 loan portion until the project is complete. The Certified Lender will sell its bond and fund its loan when the c.o. is issued. Interest and fees on the bridge loan can be included in the project costs to be financed.

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Process

Call your CDC and talk to a loan officer to discuss your project. Talk to your bank of account to see if the bank wants to participate by doing the permanent first mortgage and bridge loan. Meet with the CDC loan officer and structure the deal. Submit the CDC application which consists basically of the same materials you will submit to your bank. Basic application materials include:

- 3 years of financial statements and federal tax returns on the company (if in existence for 3 years);
- if there is no historical cash flow ability to service the proposed new debt, submit 2-3 years financial projections;
- personal financial statement (assets and liabilities) on the owners of the company;
- written history of the business, reasons for expansion, plans;
- copy of contract of sale;
- personal history statement of principals indicating citizenship status, etc.

The CDC's staff will investigate and evaluate you and your company. The CDC will draw credit reports, do supplier, bank and trade checks, visit your existing and proposed operations/facilities; assess your credit ability and character. Once your bank or other 50% first lien lender has indicated an interest in financing the 50%, the CDC staff prepares a loan memorandum and presents it to CDC's Board which meets at least once per month (more often if necessary). Once the board approves the project, the CDC presents the application to the SBA to acquire its agreement to guarantee the CDC's bond. This generally takes a few days. The CDC then issues a commitment and your bank closes its first mortgage loan and bridge loan. You take the bank's funds to complete the project. When the project is complete, you close with the CDC and the CDC wires its money to the bridge lender. You then pay the CDC back for the SBA 504 loan. The CDC services the loan for its life.

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Advantages of SBA 504 over Conventional Financing

Low downpayment. Just 10%. Lets you preserve your cash for your working capital. Most banks will lend only 60-70% of the appraised value of the project leaving you to sink in 30-40% plus the cost of renovations plus the soft costs.

Fixed rate on the SBA 504 portion. You don't have to worry about the prime lending rate going up You can plan because you know the amount of your mortgage payments for the next 20 years.

Long term. CDC 504 loans are for 10 or 20 years. Because the CDC is in second lien position, the bank or other lender doing the 50% first lien loan are willing to lend at a longer term. Longer terms make your monthly payments lower.

Low interest rate. Even with all the fees and closing costs included in the rate, it is still a low rate for a subordinate mortgage loan, particularly for small business. The blended rate as between the bank portion and the Certified Lender's 504 portion makes the project affordable for you.

For the banker wishing to participate as the 50% lender, you get CRA credits; you lend at a lower loan to value ratio; you keep a growing customer happy; you have lower risk because the SBA 504 loan is in second position behind you. The community gets the advantage of keeping or attracting a healthy, growing small business that will be creating jobs and doing other wonderful things in the community.

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You may also wish to visit the SBA website at www.sba.cloy/financing/sbaloan/cdc504.html for more information.

SBA 504 Loans are a Win-Win for Everyone!

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SBA 504 Loan Program More Attractive Then Ever for Banks and Borrowers

Merril Ferber, Director Communications & Outreach
National Association of Development Companies (NADCO)

The Small Business Administration (SBA) 504 Loan program deserves serious consideration when small business owners arrive looking for financing to expand current facilities, purchase commercial real estate or refinance an existing loan. This government-guarantee, loan program is designed to make job creation and economic development possible by providing long-term, fixed rate financing to small business owners who are investing in their companies and adding staff.

A small business that is investing in a permanent facility is often entering into its largest business-related loan, and in many cases, an SBA 504 loan becomes the basis for an entire banking relationship. Lenders have an opportunity to cultivate additional accounts and receive additional interest income from various sources. More importantly, by participating in SBA 504 loans, banks can mitigate credit risk, manage overall lending limits, and manage liquidity, while strengthening core earnings.

Since 504 loan size is linked to job creation, in general, a small business can borrow \$65,000 in SBA 504 loan funds for each job created and/or retained within two years. As growing businesses are typically adding staff as they expand and move to larger facilities, they are excellent candidates for 504 loans.

Most small businesses are eligible for 504 loans. In fact, business size was recently increased late last year to allow even more small businesses to qualify. An eligible small business must be operating a for-profit company that has a tangible net worth of less than \$15 million and profit after taxes of less than \$5 million. Also, the business must occupy at least 51% of its property for existing buildings and 60% initially of a newly constructed facility - increasing to 80% occupancy within two years. Two or more small businesses can receive an SBA 504 loan if they combine to create a real estate holding company to meet occupancy requirements. This provision works especially well for professional office buildings.

There is no limit to the total project cost for an SBA 504 loan; however, the SBA-guaranteed portion is limited to 40% of the project cost with a dollar cap of \$5,000,000 depending on the type of project. 504 loans can go as high as \$5,500,000 for eligible manufacturing projects and for projects that incorporate energy saving technologies for sustainable design. Project costs can also include certain soft costs including architect/engineering fees, interim interest and appraisal/feasibility studies. The 504 loan program will now allow for total projects in the range of \$10 to \$20 million for purchase price or construction costs for small business borrowers.

Take a look at an article published by the Office of the Comptroller of the Currency in May of 2010, "[Small Business Administration 504 Loan Program: Small Businesses' Window to Wall Street.](#)" It provides an excellent overview of the program.

SBA 504 for Refinancing Existine Debt

SBA 504 loans can include a limited amount of debt refinancing, and recent legislation provides additional authority for qualified debt refinance and provides capital to pay business debts through September 2012. SBA guidelines are currently pending; however, this may be a free-standing financing and need not be a part of a regular SBA 504 expansion project. Based on the language in the recent legislation, to qualify for this new refinancing provision, the existing debt must:

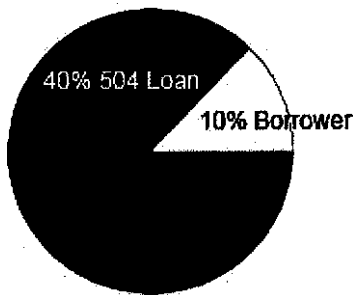
- Have been incurred not less than two years prior to the date of the refinance application;
- Be a commercial loan and not subject to any Federal guarantee;
- Have been used to acquire fixed assets which would have been eligible for financing under the regular 504 program and these assets provided to the lender as collateral; and
- Have been current for at least the past year before applying for refinancing.

The new financing may not be more than 90% of the value of the collateral securing the loan, subject to additional borrower contributions if necessary to attain the LTV. Also, the borrower must have at least a 2-year business history and the amount of the financing is limited to an amount equal to \$65,000 per employee or the borrower must meet the usual job creation/protection rule.

In addition to debt refinancing, the borrower may also use specified and itemized amounts to pay business expenses, but no part of the financing may be used for non-business purposes.

Financing Structure

The SBA 504 loan program structure is straightforward. A bank or third party lender is in a first lien position and provides 50% of the project cost. The SBA — through a Certified Development Company (CDC) — is in a subordinate lien position and provides up to 40% of the project cost. The small business borrower injection is between 10-20% depending on loan specifics.



If the project involves a special purpose building or if the borrower is a startup company, the down payment increases by 5% increments. For example, if a loan is for a single-purpose building and the company is a startup, the borrower injection rises to 20%. Collateral is typically project specific which leaves working assets available for future credit needs.

There are virtually no restrictions on the bank's loan with respect to structure or pricing. Rates can be fixed or floating. In fact, the pricing on the interim or bridge loan can be structured to reflect the greater risk during the construction phase. The only stipulation as part of 504 project financing, is that the bank's loan must be for at least 7 years for a 10-year 504 equipment loan and at least 10 years for a 504 real estate loan. The bank does its own underwriting and sets its own terms, interest rates and fees. There is a one-time fee of 0.5% of the bank loan that is paid to SBA as a program participation fee.

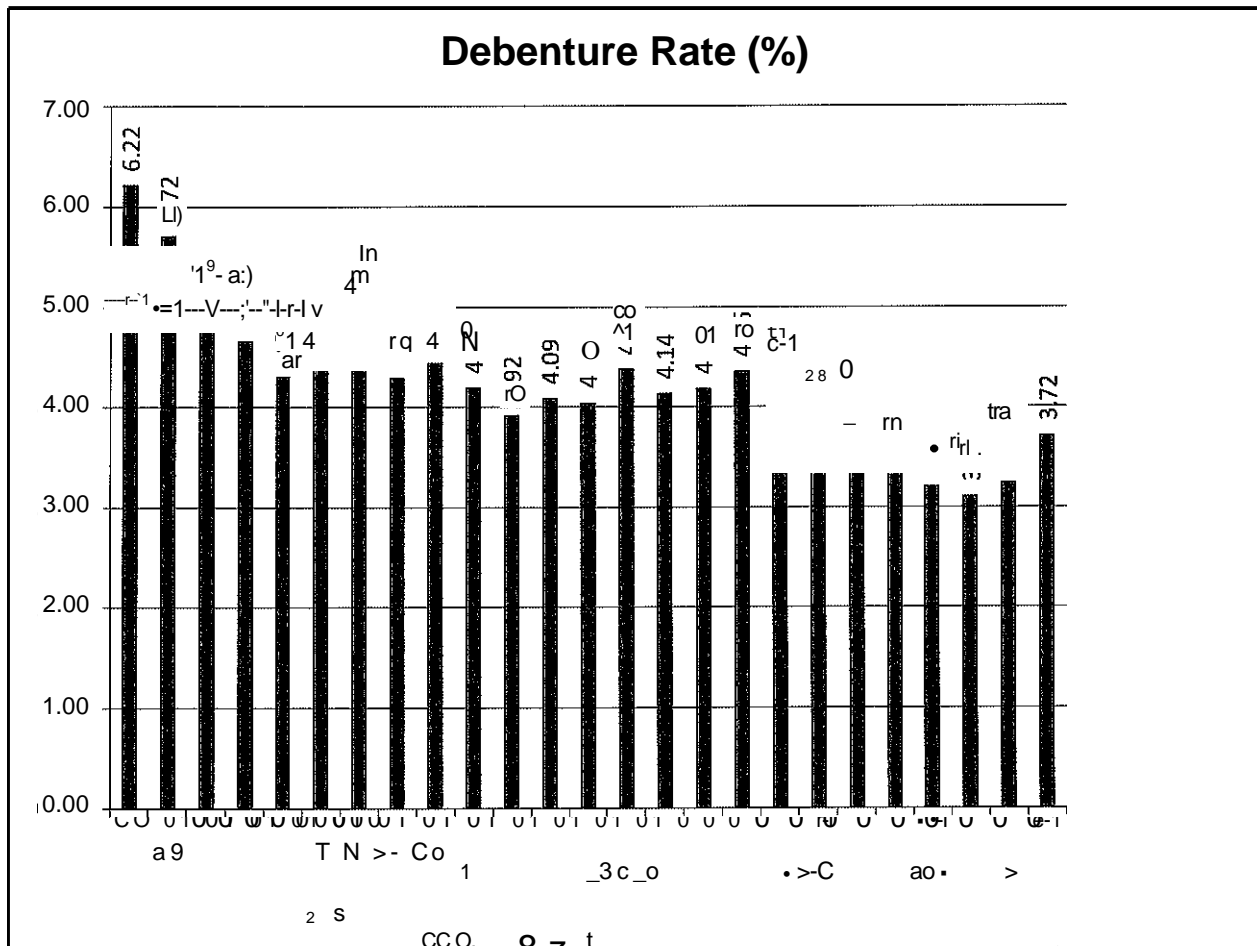
Once a 504 loan is approved by a lender, the application must be approved by the CDC's board of directors or its credit committee and submitted to the SBA. Once the loan is approved by the SBA, (usually in a few days) the bank receives a commitment, subject to specified conditions, to provide the takeout 504 loan.

During construction the bank funds the entire project balance minus the borrower's injection, however, within 30 to 60 days of project completion, the 504 loan will provide takeout financing thereby reducing the bank's

exposure to 50% in the event of default. For equipment purchases, the takeout loan is paid based on delivery and installation. In most cases, the SBA can only collect on its 504 loan collateral after the lender is paid in full.

The CDC works with the small business borrower to process, approve, close and service the 504 loan. 504 loans are funded by monthly bond (debenture) sales to investors on Wall Street. The SBA's Central Servicing Agent wires the proceeds to the banks taking out the 504 loans and provides amortization schedules to all borrowers within a week.

When reviewing the debenture sales for the bonds sold to fund SBA 504 loans, you will see that the rates dropped into the low 4% range in 2009, fell to a record low of 3.11% in October 2010 and had an uptick in November and December to end 2010 at 3.72%.



The actual interest rate the borrower pays is calculated based on the debenture rate for the month the loan funded, a CDC fee of .625%, the Central Servicing Agent fee of 1% and the SBA Borrower Fee that changes each year. You can see that the SBA 504 loan offers extremely attractive interest rates for 20-year financing. When added to the bank's interest rate on their first lien, the blended rate and 20 year term offers real advantages to the borrower.

Benefits for Banks

If a project looks good but there are lending limits to consider, a credit enhancement is required, or the customer only wants to pledge the asset being financed, a 504 loan can be the solution. Banks advance only

50% of a project cost at the beginning of permanent financing and this 50% interest can be liquid if needed thus providing excellent flexibility for managing a bank's balance sheet. Since the bank will have to manage risk during the interim construction loan, adequate care must be taken to address all issues of security positions and any related concerns at closing.

Also, with 504, smaller banks can handle larger projects and larger banks can limit their exposure to certain industries and/or to a particular borrower. The reduction of CRE loan concentration on the balance sheet also reduces regulatory concerns. Ninety percent financing also means that more of the customer's funds remain on deposit. The bank is able to earn fees and interest on the interim loan, and generate fee income from sale premiums and loan fees if it chooses to sell the first mortgage loan in the secondary market. Banks that participate in SBA 504 loans are eligible for Community Reinvestment Act (CRA) credit on most projects.

Benefits for Borrowers

The small business owner not only gets the tax benefits and appreciation on the real estate, but also locks in occupancy costs for the long term with financing tailored to the owner's needs. In addition, with financing available for up to 90% of the project cost, SBA 504 loans offer an affordable down payment, enabling businesses to conserve working capital and retain liquidity to meet operating needs. The 504 program fees are also financed in the loan and therefore do not represent out-of-pocket expenses for the borrower.

SBA 504 loans are long-term, fully amortized financing. This enables a small business owner to avoid risky loan call provisions while enjoying lower monthly loan payments. In fact, current effective interest rates are coming in below 5% which is an extremely attractive rate for long-term commercial money. CDCs handle all of the Small Business Administration paperwork and are always available to answer all technical or programmatic questions.

Benefits to the Community

The National Association of Development Companies (NADCO), the trade association representing the Certified Development Company (CDC) industry, commissioned the first formal assessment of the SBA 504 loan program's economic impact at the national level in 2007. The study, which was conducted by Applied Development Economics, Inc. and California State University, Chico, found that the 504 Loan Program very clearly provides a cost effective means by which to generate new business activity for the national economy.

As an example, applying the survey results to the more than 15,000 businesses who received 504 loans nationally during the two year study period (2003-2005), the program supported the net growth of 54,000 jobs and about \$4.6 billion in added labor income. Economic multiplier effects from the increase in direct economic activity contributed to the addition of another 66,000 jobs and \$4.5 billion in wages and salaries. In addition to significant business generation, the study found a corresponding increase in federal, state and local tax revenues that were many times greater than the funding required to administer the program.

The study concluded that in actual dollars invested, the financing provided to small businesses by the 504 loan program through CDCs represented a **\$94.00 return per dollar of program cost**— an exceptional return on investment. The complete [SBA 504 Economic Impact Study](#) and additional information on the SBA 504 loan program are available on the NADCO website: www.nadco.org.

The SBA 504 loan program is a win-win scenario for the bank, the small business borrower and the community.